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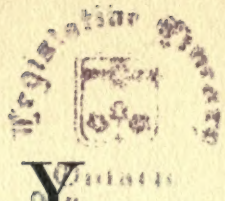

MONETARY ECONOMICS

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BY

W. W. CARLILE

AUTHOR OF 'THE EVOLUTION OF MODERN MONEY'
'ECONOMIC METHOD AND ECONOMIC FALLACIES,' ETC.

LONDON
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1912

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PREFACE

WHAT was intended at first as a preface began soon to assume such proportions that it has been converted into the Introductory Chapter. Here, I need only say a word or two as to the general divisions of the book.

Definition is plainly impossible when the meanings of all the principal terms of the science are still the subjects of controversy. Yet we must have some guiding principle in regard to the use of these terms. That principle I have endeavoured to set forth in chapters one to four inclusive. On this follows some criticism of the theory of the Margin and of Marginal Utility in two chapters, succeeded, however, by three chapters on Value, in parts of which the criticism is continued. This may be said to close the first part of the book, though it is not formally divided into parts. Chapter ten is devoted to a summary of the reasoning up to that point. In the following four chapters Money and Credit are dealt with, then the nature and the creation of wealth, and the more or less neglected theory of Demand. The book closes with some chapters that are of a more distinctly practical character.

Chapter eleven, on the origin of Money, embodies an article which appeared in the *Nineteenth Century and After*. Chapter five, on the Margin, appeared first in the *Journal of Political Economy*, and was subsequently reproduced by M. Yves Guyot in the *Journal des Economistes*. I have also drawn upon some articles contributed to the *Economic Review* and to *Mind*, and have to thank the editors of all these journals for permission to make use of these contributions here.

W. W. C.

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MONETARY ECONOMICS

INTRODUCTORY

RECENT DEVELOPMENTS OF OPINION ON THE MONETARY QUESTION

Mr. Hartley Withers.—Up to the beginning of the present century, at any rate, the explanations of the genesis of money were all of one type. The monetary substance or substances were said to have been selected for the performance of their functions on account of their homogeneity, portability, divisibility, and so on.[1] Quite a considerable number of recent writers now take an altogether different line. Among them may be mentioned Mr. Hartley Withers, the late city editor of *The Times*, whose book, *The Meaning of Money*, is generally acknowledged to be the best work on the Money Market since Bagehot's *Lombard Street* was published. Mr. Withers does not, indeed, part company with the old view altogether. At the same time the characteristic of gold on which he lays stress as having gained for it its present position, is not any of these currently enumerated as above stated, but is, on the contrary, its 'acceptability.' 'It is the universal acceptability of gold,' he remarks, 'in civilised communities that gives it both its popularity in the shape of sovereigns, and its importance as

[1] M. de Foville, in reviewing *The Evolution of Modern Money* by the present writer, in the *Economiste Français*, after referring to the Austrian doctrine which affirms the absolute universality of the relations between the increase of supply, and the decrease of value, remarks :—

'M. Carlile admet sans résistance ce *decrescendo* quand il s'agit du pain ou de la viande, de l'eau ou du vin. Mais, il estime qu'il n'y aurait pas d'étalon monétaire possible si cette loi était générale ; et c'est précisément parce que, suivant lui, l'or y échappe complètement, que l'or était prédestiné à devenir l'étalon definitif du monde civilisé. La distinction est nouvelle et il faut la prendre pour ce qu'elle vaut.'

a wheel in the machinery of credit.' [1] And again, 'The only currency that is of practical and everyday importance, is that which is 'endowed with the virtue of universal acceptability. . . . And the fact cannot be gainsaid that gold is the one commodity which is universally, and at all times, acceptable in civilised communities.'

Professor Kinley.—Another writer who is to be reckoned as, to some extent at any rate, an acceptor of the newer view of the origin of money, and of the nature of value, is Professor Kinley of the University of Illinois. In his book, *Money*,[2] he asserts with emphasis, that 'The first use of money did not arise from any agreement among men.' [3] In a later passage again, he argues as follows: 'There is still another reason for believing that the annual production (of gold), however large, cannot cause any great change in the purchasing power of the stock already on hand. The product, whatever it is, finds its way into the world's business through the banks. The first effect of an increased supply is to stimulate discounts, and to cause an expansion of business done on credit. The result, of course, is to increase the supply of goods offered for gold,' and thus presumably to make them cheaper. I had put the case,[4] as some of my readers may remember, in very similar terms, remarking that 'When the produce of African or Australian mines comes home nowadays, it finds its way first into the vaults of the Bank of England, and, practically, only gets drawn out and passes into circulation in as far as it is engaged in increasing the circulation of commodities, and in thus balancing, or more than balancing, its own increase.' [5]

Professor Keasby.—In the *Quarterly Journal of Economics* (1903) there is an article written by Professor Keasby of Brynmawr College, Pennsylvania, entitled 'Prestige Value,' which is of some interest in the present connection. The writer affirms very distinctly indeed the opinion that the true explanation of the fact that the precious metals have attained the monetary position in the world is to be found,

[1] P. 21. [2] New York, 1904. [3] P. 17.
[4] *The Evolution of Modern Money*, pp. 168, 169. [5] *Ibid.*, p. 301.

not in their supposed selection for the purpose of money owing to reasons of convenience, but because they are found to have achieved, from natural causes, comparative stability of value. After remarking in the course of his article, that the desire to accumulate wealth, and to be accounted rich, create an insatiable desire for certain classes of goods and that such goods consequently, unlike other goods devoted to immediate consumption, 'maintain their value under accumulation,' he goes on to say, near the close, 'The precious metals were chosen to serve as standards and media of exchange, not, as so many have affirmed, because they were useful, and at the same time convenient for the purpose (in fact, however convenient, if the precious metals were merely useful in the narrow sense of satisfying immediate wants, they could not have served as standards at all), but because they possessed prestige value.' Prestige value, whatever else it is, is thus, in Professor Keasby's view, the sort of value that can be 'maintained under accumulation'; that is to say, the sort of value that, to all appearance at any rate, does not necessarily fall as supply increases. It is, moreover, the value that is generated by the insatiable desire that can arise in the case of goods that are suitable for the display of wealth; that is to say, in the case of goods that partake of the nature of ornament. No doubt both of these writers arrived at the views they have expressed altogether independently. When an idea is in the air, it is strange to note how it finds expression more or less simultaneously, in very various quarters. That it does so may, however, surely be taken as creating some sort of a presumption in favour of its validity.

Professor J. B. Clark, 'Reciprocal Value.'—As regards the bearing of the new view of the genesis of money on the theory of value, I had occasion to call in question the validity of the theory which Mill, among others, had put forward as self-evident, the theory that any commodity can be valued in terms of any other commodity, that 'All values,' consequently, 'could not rise together any more than a hundred trees can all overtop one another.' In commenting on

this view, I remarked that 'In the discussions of the practical world, we assume every day that all values can, and do, rise together. . . . If the doctrine (that they cannot) were true, there could be no general increase in the wealth of the world, or of any given country, as the general wealth, we know, is but the name for the sum of values.'[1]

At the date when the above was written, I had, so far as I am aware, this line of criticism all to myself. That, however, is the case no longer. Some other economists have begun to wake up to a recognition of the inadequacy of the accepted theory. Among the number is the eminent American writer, Mr. J B. Clark, to whose theories I have had a good many occasions to refer in the succeeding chapters of this work. Mill's theory he styles the 'reciprocal value theory,' and after referring to it, curiously enough, as if it were, in some circumstances, valid, he goes on to say, 'There is a sense, however, in which values are not merely reciprocal, for it is possible to get an absolute unit of value by means of which we can add all values and get a sum total. If article A is worth half of article B, and a third of article C, this fact enables us to state the one in terms of the other two, but it does not enable us to get the sum total of the value of all three. Reciprocal comparisons yield no sums. If, however, the value of A, B, and C can be measured in something that is distinct from them all, we can get the sum of the value of these three things.'[2]

Professor Clark, it will be seen, here speaks as if there were two radically distinct sorts of value that are both valid. That, of course, cannot be so. It is the last-mentioned sort alone that shows itself in any degree in accord with the common sense of the practical world. Professor Clark's desiderated unit, in which we are to measure the value of every economic good, we are told, is 'the social cost of acquisition.' That does not seem to bring us much farther ahead. Turn over a few pages, however, and we find that 'Price is an indication of the social cost of acquisition.'[3] Professor Clark's real view,

[1] *Evolution of Modern Money*, p. 317.
[2] *The Distribution of Wealth*, p. 357.
[3] *Ibid.*, p. 391.

therefore, when stripped of its abstract verbiage, appears to be that the value of anything is measured by the amount of the monetary substance that it will fetch, and not, of course, by the amount of anything else, such as wheat, potatoes, or iron; and that is substantially the view for the validity of which I have contended.

Those who still hold to the 'reciprocal' theory do not perceive, I think, how far it takes them. If you maintain that any one commodity is just as good a measure of value as any other, including the standard commodity itself, in other words, if you maintain that the value of a thing is what it will fetch in wheat, potatoes, or iron, just as truly as what it will fetch in gold, then not only is it, of course, impossible to hold that the value of gold can be absolutely steady, but it is, further, impossible to hold that it can be any steadier than the value of wheat or potatoes or iron. A fluctuation of ten shillings a quarter in wheat would then involve precisely the same degree of variation in the value of gold as it would in the value of wheat itself. That is all the metaphysics of bi-metallism. It runs counter to every assumption of the business world. There is no banker, no tyro in finance even to be found anywhere who looks on the value of everything as subject to equal degrees of fluctuation. Every banker, on the contrary, has in his mind a sort of hierarchy of things saleable and purchaseable ranged in accordance with their relative approximations to stability in value. He thinks of stability in value in terms of 'liquidity as an asset.' Among commodities the finished article is fairly certain to be less liquid as as asset than the raw material, which has of necessity a wider market. Gilt-edged securities are more liquid—that is, more stable in value—than any commodity, and the best bills of exchange are more liquid even than they. At the summit of the whole series, however, stands gold. Nothing can be conceived of as an asset more liquid than gold. To 'realise' the value of anything is our word for exchanging it for gold. It may be that, as a noumenon, gold fluctuates, and even that it fluctuates just as much as anything else does. In the world of phenomena, how-

ever, it certainly presents the appearance of not fluctuating at all. Granted that this is all appearance only, it still remains a matter of first-class interest to render a reasonable account of it.

M. de Launay.—A recent French writer again, M. de Launay, who treats the subject statistically, finds the old theory at many points defective. The famous doctrine of the appreciation of gold, the theoretical basis of bimetallism, is, of course, a corollary of that theory. If commodities are all on a par with each other as measures of value, and if gold is used as the measure owing to nothing whatever but the fact of its arbitrary selection, then, of course, it follows that a rise in the price of anything may be interpreted as simply equivalent to a fall in the gold in which it is priced; and hence it is argued that as gold becomes more abundant in the world, prices generally must, and do, go up. M. de Launay, however, arrives at conclusions that conflict more or less with that conception. 'One is no longer so very sure,' he says, 'that the annual addition of a certain stock of new gold to the previous stock must mechanically and automatically, as has often been maintained, lead to a fall in gold, a rise in prices, and a decrease in interest.'[1] Of the gold industry, he remarks that 'Alone among industries it has no need to trouble about the sale of its product. This product flows off (at least apparently) in unlimited quantities, and at an unchanging price.' The appreciation of gold then, in his view, seems to be something that, like the gods in the philosophy of Epicurus, must in some sense have existence accorded to it, but existence nevertheless that carries with it no trace whatever of casuality in mundane affairs.

In regard to the prices of metals generally, he furnishes us with a table,[2] on which he bases an 'empirical law,' which he regards as of much interest and importance. It is nothing less than this, that the value of metals, for the most part, rises, instead of falling, with the increase of supply. It applies, in recent years, he endeavours to show,

[1] *The World's Gold*, Eng. trans., p. 203. [2] *Ibid.*, p. 214.

to copper, iron, lead, tin, and zinc, and unquestionably, in their case, the price and the output have risen together. There is, however, nothing very surprising in this. Demand, in the case of metals, or of anything else, may easily enough, over a considerable period, be sufficiently strong and well sustained to cause such coincident increases. M. de Launay, however, conceives himself to have lit on a discovery of quite mysterious import. He goes on to apply it by analogy to the case of gold itself. The increase in the output of gold, he observes, in the recent period has been greater than in the case of any other metal. It, therefore, seems to him arguable that its purchasing power has been increasing also, that is to say, that, while so many economists have been telling us that it has been depreciating, it has really been appreciating. When a man starts theory-building on the strength of inferential but invisible variations in gold values, he can apparently arrive at any conclusion that his fancy dictates.

The Title of the Book—Monetary Economics.—In naming this volume *Monetary Economics*, it is necessary to observe that the word 'Monetary' is rather to be looked upon as a Homeric epithet than as a differential adjective. There is no economics that is not monetary. Adam Smith, in his polemic against the mercantilists, was led to assert—no doubt with a certain measure of truth—that the real wealth of a country did not consist in the amount of gold and silver that it possessed, but in the innumerable commodities for which this gold and silver would ultimately be exchanged. Mill pushed this line of thinking much further. He affected to deal with economic questions in the first part of his work without introducing the conception of money at all, but never, of course, for a moment succeeded, as every line that he wrote, from first to last, was permeated by monetary assumptions. 'He takes,' as I remarked, 'the whole terminology of "cost," of "price," of "buying," of "selling," and so on, all of them words and thoughts that are dependent on a standard of value for their existence, and interpolates them into an imaginary

state of things in which, by hypothesis, no standard has yet been born.' [1] If, however, I went on to argue, my view of the genesis of money was the valid one, then the notion of its unimportance to the scientific economist was seen at once to be an absurdity. Mill indeed says, as we know, that there cannot be a more insignificant thing in the whole economy of society than money. 'Rather,' I urged, 'the truth is that we cannot move a step towards the elucidation of any (economic) problem without first studying the nature and operation of the standard substance.'

Professor Veblen.—Professor Thorstein Veblen,[2] the most brilliant of the younger American economists, has arrived, I observe, at conclusions similar to mine in regard to the bearing of the evolutionary origin of money upon economic theory, and sets them forth with admirable force and insight. He had occasion, in the *Political Science Quarterly* of June 1909, to criticise a book on *The Rate of Interest*, by Professor Irving Fisher. Professor Fisher belongs to the Marginal Utility School, and is, consequently, full of the tiresome project, characteristic of the writers of that school, of attempting to treat economic questions in a fashion that takes no account of money. On this basis he deals with the subject of interest. 'Interest,' however, urges Professor Veblen, 'is a business proposition, and is to be explained only in terms of business, not in terms of livelihood, as Mr. Fisher aims to do. . . . Interest is a pecuniary concept, having no validity (except by force of an ambiguity) outside of the pecuniary relations of the business community, and to construe it in other, presumably more elementary terms is to explain it away by dissolving it into the elements out of which it is remotely derived, or rather to which it is presumed to be remotely related. The phenomena of modern business, including the rate of interest, can no more be handled in non-pecuniary terms than human physiology can be handled in terms of the amphioxus. . . . There is (probably) no science except

[1] *Evolution of Modern Money*, p. 325.

[2] Of the Stanford University, San Francisco.

economics in which such an endeavour to explain the phenomena of an institution in terms of one class of the rudiments, which have afforded the point of departure for the growth of the institution, would be listened to with any degree of civility. The philologists, for example, have various infirmities of their own, but they would have little patience with a textual critic who should endeavour to reduce the Homeric hymns to terms of those onomatopoetic sounds out of which it is presumed that human speech has grown.'

In the writings of the Marginal Utility School he remarks elsewhere :[1] 'The whole money economy, with all the machinery of credit and the rest, disappears in a tissue of metaphors, to reappear theoretically expurgated, sterilised and simplified into a refined system of barter, culminating in a net aggregate maximum of pleasurable sensations of consumption.' As a general description of the economics which we have been accustomed to see issuing from the universities during the past thirty or forty years the characterisation leaves little to be desired.

Professor Wesley Mitchell.—Another Californian professor, Mr. Wesley Mitchell,[2] takes up the parable in the *Journal of Political Economy* of March 1910, in a paper entitled 'The Rationality of Economic Activity.' He deals with the subject on the same lines as Professor Veblen, and also in an interesting and enlightening manner. 'There can be no more convincing proof,' he remarks, 'of the vital rôle which economic concepts play in human life than the egregious blunders into which economists have stumbled through imputing the use of full-fledged modern concepts to primitive man. From the scientific point of view, the theorist commits an error no less serious when, in accounting for the current situation, he treats the concepts which modern men have gradually learned to use as if they were a matter of course, an integral part of a man's native endowment, something generically human.'

[1] *Journal of Political Economy*, November 1909.
[2] Of the University of California.

He quotes Mill's strange outburst about the supposed insignificance of money, and remarks that, as the result of this view, money was relegated by Mill to separate chapters placed after the chapters dealing with value and distribution. Marshall, he remarks, does the same, leaving money over nominally to his second yet unpublished volume.

Clark and Fisher, he thinks, are more unreal than Marshall, and this is because the latter more continually postulates the conditions of the modern money economy. At the same time, Marshall 'fails to see how substantial a factor in shaping the whole modern situation has been that seemingly superficial thing money. Such a grasp upon the facts indeed becomes possible only when economic problems are seen from the evolutionary view point.'

'At present,' he remarks in another interesting passage, 'we remain ignorant because we have leaped past pecuniary concepts in our haste to reach the Marginal Utilities assumed to lie behind them. . . . Pecuniary concepts are much more than a set of empty symbols which men use merely to facilitate their 'thinking,' but which do not alter the substantial features of economic activity. Consequently, the theorist who leaves them out of account in order that he may get an unobstructed view of the realities for which the symbols stand, becomes superficial when he means to become profound.'

In the following passage Professor Mitchell furnishes us with an excellent recipe for the conversion of the ordinary common-sense language of men of business into the special speech of the marginalists. 'This formulation,' he says, 'of the mental operations of an ideally perfect money-maker can be converted into a passable formulation of Bentham's hedonics by merely turning pecuniary into psychological terms. Substitute pleasure for profit, and pain for loss ; let the unit of sensation stand for the dollar, replace accounting by the hedonic calculus, interpret self-interest as the maximising of net pleasures instead of net profits, and the transformation is complete.' Thus furnished, no doubt most people of average intelligence could

turn out the new economics in unlimited quantities if the result were such as to repay the exertion.

The Cambridge Economics and Socialism.—In Cambridge, on a recent occasion, Mr. Sidney Webb, after giving expression to the view that the progress towards collectivism had been steady throughout the nineteenth century, went on to remark that the Cambridge economists had led the way that Socialists were following. The statement created some surprise and a good deal of dissent. Substantially, however, it contains a large measure of the truth. The school do not indeed avow themselves Socialists; neither, however, for that matter, did Ricardo, yet Ricardo's labour value theory, as we know, became the basis of Marx's system. The tendency of the whole line of marginal utility reasoning now dominant in Cambridge, and to some extent also in Oxford, is to create an atmosphere in which socialistic projects and ideals can live and breathe, while in an atmosphere charged with monetary conceptions they immediately wither and die away.

Take, for example, the treatment of the important conception of profits by the most authoritative member of the school, Professor Marshall. Judicious buying to be followed by advantageous reselling plays, of course, a part of the utmost significance in the creation of wealth in the view of the ordinary man. It is a fact in human life, however, that cannot anyhow be made to fit itself into a collectivist system of doctrine, and to the marginal utility theorists it is also alien and unwelcome. The attempt accordingly to bring profits somehow under the heading of 'The Earnings of Management,' and so really to explain them away altogether, is found to be a well-marked feature of Professor Marshall's principles, involving a vast quantity of very difficult and very elaborate ratiocination. If, however, profits are nothing but 'earnings of management,' then they are merely the reward of one form of salaried labour, and if we can persuade ourselves that all wealth is created by salaried labour and nothing else, then we are well on the road towards Socialism already.

We find again the university economics full of the all-pervading conception of the necessary proportion that should be found to rule between pain, effort, or sacrifice on the one hand, and wealth production on the other. At bottom it is a theocratic conception of life, with the Deity kept carefully in the background. It stands in sharp contrast, at any rate, to the more valid evolutionary view. The latter treats wealth creation as one form of success in the great competitive struggle that rules throughout all Nature. In view of the existence of this struggle, we should have to substitute for pain and effort, vigour, efficiency, foresight, and individual initiative. Between these latter and wealth creation indeed, a proportion is readily enough discernible. To recognise and to emphasise that fact, however, is to sign the death-warrant of every collectivist theory.

CHAPTER I

AN ALTERNATIVE TO THE DEFINITION OF TERMS

Words fail in their end 'when they apply the common received names of any language to ideas, to which the common use of that language does not apply them.'—LOCKE, *Essay on Human Understanding*, bk. III. ch. x. § 23.

IT is a common practice among the economists to devote some preliminary chapters to the definition of the terms that they propose to make use of in the course of their discussions. If we attempt to follow it, however, we encounter this difficulty at the outset, that these definitions are, practically all of them, the subjects of controversies that are as yet unsettled. The difficulty lies deep in the nature of definition itself. The man who could define 'Life,' said Whewell, would know more than all the biologists. Sidgwick saw in the pursuit itself, the sole useful end of the search for definitions. Humanity has been seeking for an adequate definition for the word 'Cause' ever since speculative thought first emerged on the shores of the Ægean. At the same time, every one who can use the word Life or the word Cause in his intercourse with his fellows with a fair degree of accuracy, must be said in some sense to know their meanings. We are face to face therefore with the remarkable fact that it is possible to know the meaning of words while yet it is impossible to define them.

In the view of the most recent school of philologists, there was a period in the history of the human race when there were no words at all that could be said to have a separate, independent meaning of their own; all, on the contrary, were tangled together in immense word sentences such as Aglekigiartorasuarniarpok, which may, perhaps,

be translated 'He goes away and exerts himself to write'; [1] and this fact corresponds to the well-recognised truth of psychology, that it is not individual things that are originally given to us by sense, but a total presentation which thought afterwards converts into separated and localised objects, attributes and events.

'It is an utter impossibility,' says Dr. Jespersen,[2] 'for a savage to think of "knife," for instance, by itself: his power of abstraction is not sufficiently developed, but he can perfectly well say "give me that knife," or "he plunged the knife into the hart."' After abstraction has done its utmost, however, there still remain innumerable words which cannot be said to have had conferred on them a definite self-dependent existence apart from their context. Such words as Cause are among the number, and a recognition of the fact may perhaps assist us to comprehend the difficulty or impossibility of defining them while yet it is possible to use them with accuracy.

Suppose, again, to look at the subject in another light, that we have found a definition for a philosophical or economic term, with which we are fairly well satisfied, we may still have to inquire what is the ground of our satisfaction. Say that we accept the definition of Capital, which runs to the effect that it is 'wealth destined to the production of fresh wealth,' [3] we have next to ask whether we can offer any proof of its validity to an inquirer who is disposed to dispute it. We certainly have not got the definition by a revelation from heaven. What, then, is the foundation of the faith that is in us? What we universally do in such circumstances is to look for an illustrative example. We see a box of cigars, say, in a tobacconist's shop window, and we ask ourselves, 'Is that box of cigars now capital?' We answer, 'Yes, it is'; because the tobacconist hopes to sell it at a profit, and so to create for himself fresh wealth by means of it, and, in these circumstances, the living speech of business assigns to an

[1] Lubbock, *Origin of Civilisation*, p. 279.
[2] *Progress in Language*, p. 348.
[3] Practically Mill's definition.

object so situated the character of being 'Capital.' We see it afterwards on the table of his smoking-room in the evening, and again we ask ourselves, 'Is it capital now?' We answer 'No,' because he does not now mean to use it in the production of fresh wealth, but for his personal transitory enjoyment; and, again, popular business language does not assign to an object so used the name of 'Capital.' In both cases thus, when we go behind our definition to look for the principle on which it rests, we find ourselves inquiring whether or not it conforms to the popular use of the word defined. Can we then formulate a general proposition to the effect that a definition in economics to be valid must always be in conformity with common business usage? My answer, I may say at once, would be in the affirmative, and the three chapters that follow will be devoted to an attempt at establishing that position.

CHAPTER II

THE APPEAL TO THE COMMON AND PRACTICAL USE OF LANGUAGE

A GOOD many economists appear to be of opinion that they can settle any difficulty that may arise in connection with the definition of their terms by a method that cuts the Gordian knot. They will take up, they say, the position to start with that it is their intention to define their terms in the sense in which they mean to use them, and they contend that if they adhere consistently to that sense, then they will have done all in the matter that can be reasonably expected of them. We meet even with writers who tell us frankly that they are using such words as 'rent,' 'profit,' 'interest,' and 'gain' in senses of their own—senses which 'are entirely different from that sanctioned by common usage.'[1] The leading economists indeed do not commit themselves to utterances so crude as this. When, however, we find Jevons proposing to drop altogether the use of the word Value, because of its alleged ambiguities, and Mill proposing to do the same with no less a word than the word Cause, we are aware of the existence of an attitude of mind on their part towards the conceptions of ordinary speech which is not dissimilar to that of the writers just cited.

An American economist of note, Mr. F. B. Hawley, makes the very interesting statement that General Walker once remarked to him,[2] 'There is only one permissible use of an economic term, and that is the right one.' We

[1] Macfarlane, *Value and Distribution*, p. 314. Pantaleoni similarly remarks, 'We are NEVER concerned to know what are the meanings attached to a term in vulgar parlance (*Pure Economics*, Eng. trans., p. 70). The small capitals are his own.

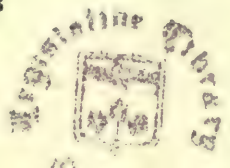
[2] *Quarterly Journal of Economics*, vol. xvi. p. 241.

find ourselves thus, here, face to face with the question whether rightness or wrongness can be justly attributed to the assignment of names, a question broached more than two thousand years ago by Plato in the 'Cratylus,' but on which, for all that, the last word has not yet been said. Walker, Mr. Hawley tells us, honestly confessed that he was unable to say how the right sense of an economic term could be ascertained.

This question of the right use of the salient terms of the subject matter with which a writer has to deal, is one that presents itself as persistently in abstract philosophy and in psychology as it does in economics. It plays a great part, too, in jurisprudence, and it can, it seems to me, be best dealt with when we take account of it, to some extent, in its bearings on all these branches of investigation. That is the course that I propose to pursue in the following chapters.

The Criterion of Truth in the Subject Sciences.—In an article in *Mind* of January 1895, seventeen years ago now, I endeavoured to open up the discussion of the present question. My first paragraph ran as follows: 'To what criterion can we appeal as final in philosophical discussion? Is there anything that, in regard to Metaphysics, or to what has lately been called Epistlemology, occupies the position that Authority occupies in regard to Theology, Precedent to Common Law or Experiment to Physics? There is, of course, the criterion of self-consistency. That, however, is only a criterion of sequence. We can show that a writer's conclusions do not flow from his premises, but what about the premises themselves? Is there any rule that we can supply that will be generally accepted as decisive one way or another in regard to their validity? There is, we find, one criterion that is frequently applied in the last resort, and often apparently with the tacit consent of all parties. That is the appeal to the natural use of language.'

Mill, I pointed out, now and then made use of this appeal in a literal and manifest fashion, calling in, on occasion, 'the man with no theory to support,' the man who conse-



quently must be presumed to be ignorant of the technicalities of philosophy or of economics, as the case might be, as the ultimate judge of the right use of philosophical or economic terms. The manner in which the appeal ordinarily presented itself, however, was of a more subtle, and at the same time, of a more far-reaching character. It underlay, indeed, the method in constant use of testing any general statement in these branches of investigation by individual instances. Hume lays it down, for example, that the Cause means nothing but the invariable antecedent. Reid answers that, if that were so, we should call Night the Cause of Day. What is this answer at bottom but the appeal to the popular meaning of the word Cause ?

A famous instance of the appeal to the natural meaning of words will be recalled by those who remember the controversy between Mill and Mansel in regard to the attributes of God. Mansel had contended that such goodness as we attribute to God ' may differ, not only in degree, but in kind,' from the goodness that we ascribe to good men. Mill rejoins : ' Here, then, I take my stand on the acknowledged principle of logic and morality, that when we mean different things we have no right to call them by the same name, and to apply to them the same predicates moral and intellectual. Language has no meaning for the words Just, Merciful, Benevolent, save that in which we predicate them of our fellow-creatures, and unless that is what we intend to express by them, we have no business to employ the words.'

The proposition that God's goodness may differ in kind from the goodness of human beings thus, in Mill's view, must be rejected as invalid, on the ground simply that to admit it as valid would be to give to the word ' goodness ' a meaning that is not in accord with popular use. Mill thus here assumes an attitude of something very like submissive reverence towards the great ethical conceptions stored up in ordinary speech by the ' unconscious cerebration of the race.'

Contrast, however, with this attitude, the attitude adopted by him in other passages towards conceptions similarly stored up in common language. There is no

difference, he thinks, between a ' quality ' and a ' sensation.' It is only the ambiguity of popular language that makes us think that there is.[1] It is only, again, he asserts, the mere ' caprice ' of language ' that makes us call one among the many conditions precedent of every occurrence its cause.' If language, however, is so full of idle caprices, what becomes of the appeal to it in such a case as that above cited ?

Mr. Henry George is another writer who occasionally makes the appeal to the popular meaning of words in a quite definite and manifest fashion, though, as we shall see, on other occasions he is far from regarding himself as bound by it. After enumerating various things that, in the special circumstances mentioned might, he thinks, be fairly ranked as capital, he remarks that if you were to take the verdict of any dozen of intelligent men, who know nothing antecedently of the subject, as to whether they might be thus ranked or not, they would all without difficulty give an accurate answer. They would all, it would be found, set down the same things, and the right things, as capital.

The same sort of appeal is found to be made every day with increasing frequency in current economic controversies, although no one seems to think it necessary to defend it in the abstract, or to attempt to formulate its underlying principle. In a recent discussion in the *Quarterly Journal of Economics*,[2] on the meaning of Capital, between two American professors, Messrs. Tuttle and Fisher, I counted up fourteen instances of it in the course of a dozen pages ; in each case the words ' The Common and Practical use ' being employed.

Professor Fisher's idea, however, of the manner in which the appeal should be made was significant and, in its way, enlightening. He put the question, he said, to a business friend, ' Do you reckon that cigar that you have in your mouth is capital ? ' The business friend, of course, said, ' No.' Professor Fisher, however, in the end, succeeded in persuading him that it really was capital, and quotes the

[1] There is surely, at any rate, this difference that a quality is one, while the sensations that correspond to it are innumerable.

[2] See vols. xviii. and xix.

fact in support of his own view that this was the case. Evidently that was not the way of appealing to the man with no theory to support, or to the man with no antecedent knowledge of the subject, as we have found Mill and Henry George doing. The question is, Why do they do it? why does the appeal take this form? The answer is that it is the appeal of theorists engaged in the attempt to formulate dictionary meanings for words to what has been called their 'occasional meanings,'[1] that is to say, to the meaning of the word when caught in the very act of imparting practical information. In such circumstances it was, of course, the business man's first impression that alone was salient. This aspect of the question, however, will have to engage our attention again later on.

It will further serve to illustrate the nature of the principle of conformity with popular usage in language if we cite a few instances of its glaring contravention. Take, for example, the following from the sphere of economics :—

M'Culloch lays down the doctrine of his master, Ricardo, that value never emerges except as the result of labour, and is always exactly proportioned to the labour expended. In reply, the question is put : What then about wine ? When you put it in your cellar, it may be worth perhaps a shilling a bottle, when you take it out a few years afterwards, it may be worth several shillings. Where does labour come in ? M'Culloch replies with refreshing audacity. It is still labour that creates the added value, the labour of natural forces ! Who is there to-day that does not regard the reply as an absurdity ? But, on what grounds ? Upon no other than this, that it violates the instinctively, though dimly recognised rule, that the word ' labour ' must be used in the discussions of economic theory in the same sense as that in which it is used in practical life. In practical life, however, the operation of natural forces is not described as labour, and neither must it be so described in the discussions of economic theory.

Take again the following example :—Mr. Henry George comes down upon us with the startling assertion that

[1] Paul, *Principles of the History of Language*, chap. iv.

'Wages are never paid out of capital,' and that 'the payment of wages never even temporarily diminishes capital.'[1] You point out in reply the case, let us say, of a gold-mining company that has paid away all its capital in wages without finding any gold, and ask: How can you make such a fact as this square with your general statement? Mr. George would answer—he does in effect, 'I am not using either the word Capital or the word Wages in the sense that you suppose. I claim the right to attach my own meanings to such words so long as I adhere to them consistently throughout my book.[2] In the sense which I propose to attach to these words my general statement is sustainable. If such a position as this in regard to economic language can be regarded as valid, then there is, of course, an end of the controversy. There is, however, at the same time, an end of economic theory. No proposition in that department of science could then be capable either of verification or of refutation, and, in that case, could any proposition be worth propounding? Those, however, who are prepared to admit that such a position in such a case is not tenable, will find that, in the end, they will have another and a much longer step to take. Consistency, I think, will force them to give in their adherence to the view that popular usage as the determinant of the meaning of economic terms occupies an impregnable position; that it is our last court of appeal, and that, without the postulation of its unimpeachableness, economic science becomes impossible.

Turn again to the discussions of abstract philosophy for a third illustrative example. Bishop Berkeley remarks: 'Sitting in my study I hear a coach drive along the street. I look through the casement and see it; I walk out and enter into it. Thus, common speech would incline to think I heard, saw, and touched the same thing, to wit, the coach.'[3] But, can we believe our ears? Does the distinguished philosopher mean to tell us that the coach which he gets into now is not the same coach which he has, up to this moment, been watching as it is driven up to his door?

[1] *Progress and Poverty*, p. 46. [2] *Ibid.*, see book I. chap. ii.
[3] An essay towards a new theory of vision, sec. 46.

Assuredly he does. If, however, the ordinary meaning of the word ' same ' may be played fast and loose with in this manner, why not that of every other word in his sentence ? The principle that underlies his use of words plainly runs counter to the convention that forms the basis of intelligible speech. Carried out to its legitimate consequence, it would render communication of every sort between man and man impossible. We are led thus to conclude that there must, at any rate, be some limit placed on the variation from common usage, which is permissible in the employment of philosophical and economic terms ; and those who think that any variations at all are permissible, have the very difficult task facing them of formulating some principle in conformity with which this limit can be assigned.

CHAPTER III

OBJECTIONS TO THE VALIDITY OF THE APPEAL TO THE COMMON USE CONSIDERED

We have arrived, then, tentatively at any rate, at the conclusion that the test of validity in the employment of economic or philosophical terms is to be found in the conformity of our use of them to the use of the same words in living speech ; that is to say, as regards economics, in the conformity of the theoretical with the business use. We have seen that every economist acts on the assumption that this test is conclusive when he is criticising the reasoning of his opponents ; at the same time, if we attempt to set the principle forth in explicit terms, we certainly cannot look for general and immediate assent. The difficulties, indeed, that its acceptance involves are, at first sight at any rate, formidable. This chapter will be devoted to the attempt to deal with some of them, and, in dealing with them, it may be possible incidentally to bring out with greater clearness the true nature of the principle itself.

Objection 1. The Alleged Ambiguity of Popular Language. —The first objection to be dealt with is the instability of meaning commonly attributed to popular language itself. Is it not notorious, it will be asked, that the popular use of economic terms is in the highest degree variable ? How then can an appeal be made to that which is in itself so unstable ? There is plainly, however, some misunderstanding here. If the meaning of such words as Price, Value, and the like was as unstable as the economists so generally assert, the business of the world could never get itself transacted. We know that millions of pounds sterling change hands every week in the Stock Exchanges in trans-

actions conducted purely by word of mouth, and that the cases in which disputes or misunderstandings arise are a mere infinitesimal fraction of the whole. That does not look as if business language were in its own place either ambiguous or indefinite.

We are liable sometimes to think of language as if its primary purpose was that of enabling us to think out abstract problems. It serves that purpose, no doubt, but such service is a by-product. Its primary purpose is to communicate from man to man the sort of information that has an immediate bearing on action, necessarily therefore information about the things and persons that have played a part, or are expected to play a part, in the changes in his environment. So long as language achieves that end satisfactorily, the thinking out of abstract problems may be left to take care of itself. There was a period, no doubt, in human history when superiority in the use of the rudimentary means of communication, whether by gestures, by pictures, or by articulate speech, was as important an element in warlike efficiency as wireless telegraphy or aeronautic scouting is expected to be among ourselves. Language first made co-operation possible, and the solitary units could hardly fail to perish out before their co-operating rivals. There have always, thus, been forces at work, from the dawn of history and long before it, calculated to eliminate any indefiniteness and ambiguity that might emerge in language when used for this, its primary purpose.

No Ambiguity in the Concrete.—It is interesting, and even astonishing, accordingly, to observe how the ambiguities vanish from economic terms when we leave behind us the reference to their dictionary meanings, and turn to the consideration of them in their applications to concrete individual cases. In connection with the word Value, an immense deal has been made of the alleged inconsistency between the meaning of value in use and value in exchange. This supposed inconsistency has been styled *par excellence* the *contradiction économique*. Professor E. von Boehm Bawerk persuades himself that it is a 'startling pheno-

menon.' But look at the use of the word in the concrete, there is no contradiction left to startle the most super-sensitive.

Coals, you say, have a greater value in use than diamonds, while diamonds have a greater value in exchange than coals. But take the case of a sack of coals worth two shillings, and a diamond worth twenty pounds in an ordinary English city of to-day. The diamond has a greater value in exchange than the coals. True, but it has also a greater value in use, for the simple reason that by taking a very little trouble you can get two hundred sacks of coals for it, and two hundred sacks have a greater value in use than one. Even without parting finally with the diamond, indeed, it will enable you to supply yourself with an immense quantity of coals. Suppose, again, the same sack and the same diamond to be found among a shipwrecked crew on a desert island with winter coming on. The sack of coals has a greater value in use now than the diamond. True ; but it has also a greater value in exchange. No one would part with it for many hundreds of such diamonds. There is no contradiction, no ambiguity whatever. All is simple and plain sailing.

We are now perhaps in a better position to understand the true nature of the appeal to common use. It is certainly not the appeal to the usage of other economists in regard to the formulation of the abstract meanings of the terms they deal with. That may or may not be important in its way. It is enough to say that it is not the matter here under consideration. That matter is the appeal that is made, as we have seen in commenting on Mr. Fisher's employment of it, when some dictionary or definition meaning is in question, to the use of the word in living speech, to its use, curiously enough, preferably by those who know nothing of economics, and who consequently have no theory to support. It is, it may be added, not necessarily the appeal from our own use to some one else's, or from some one else's to our own. It may be the appeal from our own use in economics to our own use in business. A theorist asserts, perhaps, that land is not capital ; yet the same man will

include the value of his land along with that of his other capital in making up his balance-sheet, or in any other business document or communication.

The German philologist, Paul, draws a distinction between what he calls the 'usual' and the 'occasional' meanings of words that has something in common with this distinction between the definition meaning and the living use.[1] He seems to take it for granted, however, that the 'usual' or abstract meaning is the source of the 'occasional' meanings, that the latter are mere variations of the former. The relation between the two is altogether different. Some of the commonest of our words, such as the word Cause, and the word Life, as we have seen, to this day elude the possibility of definition.

Rather is it true that the concrete or living use stands related to the definition as facts stand related to hypotheses. The man who is searching for a definition, say, of such words as Value, or as Capital, will have to try and to reject many experimental definitions before he can hope to find one that will fit into and explain the concrete use in every instance, just as Kepler, having the observed positions of Mars as his facts, had to try and to reject many hypotheses before he lit on that of an elliptical orbit for the planet which fitted and explained them. If, however, the meanings in common use are our facts, it is plain that any tampering with them is a thing that is not to be so much as dreant of.

The Term and the Context.—Another way of saying that the appeal to the common use is an appeal from the dictionary meaning to the living employment of the word, would be to say that it is the appeal from the meaning of the word when taken out of its natural environment to the meaning of the same word when we find it indissolubly involved in its context. It is safe to say that every economic term, without exception, thus taken out and isolated, can be made to present apparently contradictory meanings. It is, indeed, part of their very nature to do so. Take Wealth for example.

[1] *Principles of the History of Language*, chap. iv.

You ask, Is a mortgage for ten thousand pounds on English landed property 'wealth'? The only possible answer is 'Yes,' from the point of view of the mortgagee, 'No,' from the point of view of the English nation. Is a printing-press fixed or circulating capital? It is 'fixed' capital from the point of view of the purchaser—a printer, 'circulating' capital from the point of view of the seller whose business it is to make or to deal in such articles. Controversy still rages over the question: Is the food that is supplied to productive labourers capital or not? The only possible answer is that, from the labourer's point of view, it is not—it is consumptive goods; but from the employer's point of view it is—it is wealth destined to the creation of fresh wealth. From the national point of view it may be regarded in either light according to circumstances. Costs, Professor Marshall holds, are something that include normal profits.[1] But are not profits precisely the difference between the costs and the price realised in any given case? How then can costs include them? Looking forwards, as indeed we must do, judging by the context, in this instance, it is impossible to hold that costs include profits, but there is this much excuse for the assertion, that, when we look backwards, the case is altogether changed. The producer who has bought the factors of production, in paying for them, has furnished his profits to the seller—the costs of the shoemaker, for example, in buying leather include the profits of the tanner, so that in that case it must be held that costs do include profits. We can thus make no general statement to the effect either that costs do or do not include profits. All we can say is, my costs do not include my own profits; but, at the same time, there is no doubt that they do include certain other people's profits. In the march of affairs in the world, indeed, profits are being every moment converted into costs.

There is, it must be said in this connection, a false ideal which largely pervades the work of the economists of the modern school. They assume that an economic term should be capable of being taken out of its context and put under

[1] *Principles*, 5th ed., pp. 443, 478.

the theorist's microscope without manifesting any inconsistencies of signification. When inconsistent meanings are discovered, the writer at once makes haste to let the world know of his discovery. He feels that he is rendering a service to science by dragging the ' contradiction ' to the light of day. We saw, however, how the contradiction between value in use and value in exchange vanished when we fell back on the concrete use of the word, that is to say, when we refused to let it be taken out of its context. We have not far to look for other cases of a parallel character. Professor E. von Boehm Bawerk's lengthy criticism of the older economists in the earlier part of his *Capital and Interest* furnishes many examples. He makes Adam Smith give what he reckons are manifestly contradictory accounts of value, of capital, and of interest. On the strength of the clause, taken out of its context, ' The value which the workman adds to the material,' he would father on Smith, in anticipation, the Ricardo-Marx labour-value theory. When Smith, in a subsequent passage, expresses views palpably at variance with any such theory, then his critic pounces on the passage and exclaims, ' Here you see the contradiction.' Take the whole context together, however, and it becomes clear at once that all along nothing was further from Adam Smith's thoughts than the theory with which he is credited. He is speaking of the labour employed by an entrepreneur who pays the wages in advance of the result, and who supplies the materials. How, then, in such circumstances, could the entrepreneur have failed to co-operate in creating the value ? By the application of such methods the clearest possible economic writing could, at any time, be represented as full of contradictions.

The two Classes of Words.—We had occasion to refer above to what has been called the holophrastic stage in the development of language, a stage at which no word whatever could be thought of apart from its context. We have now in language, of course, vast numbers of words which are capable of being regarded in isolation, while, at the same time, we have a vast number of others with regard

to which the contrary is the case. The words ' gold ' and ' iron ' belong to the first class. They are the names of the same substances, and of the same substances only throughout all the world, and in all ages. Nothing can ever be gold at one moment, and not gold the next, or gold from one man's point of view, and not gold from another's. Take the word Capital, on the other hand. Practically everything that is handed over a counter in the ordinary transactions of daily life is capital one moment, and not capital the next, capital from the seller's point of view, and not capital from the buyer's. To hunt for a meaning for capital consequently that has the same sort of fixity as the meaning of gold, is to hunt for something that does not and cannot exist.

An objection has been made to Mill's definition of capital as wealth destined to the production of fresh wealth, to the effect that it introduces the intention to use a thing in a certain manner into the definition of the thing itself. Of course it does. It is part of the very nature of such things that this should happen in regard to them. Many of them take their names expressly from their purpose, from the fact that people mean to put them to a certain use. We project our intention into the very nature of the objects that we contemplate. The class of things that take their names in this way extends far beyond the range of specially economic terms. Take such an example as this. You see that piece of timber lying on the ground. Physically, it is oak, five feet in length, two inches by three in its other dimensions. That is the sum of what physics has to say about it. I use it to shift a log. It becomes, at once ' a lever.' It lies beside me as I dig a post-hole. It is now ' a fencing post.' I set it aside to burn ; it becomes ' fuel.' Its mere physical aspect is very little of a guide as to which of these three things it is. To know that we must know what is the use to which it is intended to be put. Similarly, in regard to the sovereigns or bank notes in my purse or my till ; they may be used as wages, as rent, or as interest. We do not know *what they are* economically till we know for what purpose they will be used. A doctor's carriage, it

has been truly said, is capital in the morning when he is using it to visit his patients, not capital in the afternoon when he is driving in the Park with his family. The allegation of ambiguity as attaching to economic and philosophical terms, is due at bottom to the fact that they do not, and cannot, conform to the impossible ideal of physics.

If we go back to the infancy of speculation, we find the pursuit of the physical ideal still more potent to mislead than it is with us at present. In the *Euthydemus*[1] the argument is put forward, if not as a sustainable one, at any rate as a puzzling and plausible one ; that, as gold cannot be both gold and not gold at the same time, so a father cannot be both a father and not a father at the same time ; and that, therefore, if a man is my father or your father, he must be a father to every one, including the foals and the puppies. Plato, no doubt, has it in his mind here to caricature the reasoning of the sophists, but even as a caricature his presentation of it is almost meaningless for us nowadays, so profoundly has the point of view changed ; and further, it must be said, that a very similar argument occurs in the *Phædo*, where the reasoning is certainly meant seriously enough.[2] In the *Thætætus* one of the interlocutors seems to think that such words as 'more' and 'fewer' possess self-contained meanings that should be consistent with themselves in all circumstances, and imagines that he discovers a contradiction in the statement that six is more than four, but less than twelve, because the predicates 'more' and 'less,' which ascribe contradictory qualities, are affirmed of the same thing at the same moment.[3]

How Things, Physical and Mental, obtain their Names.— In order to get at the bottom of the distinction illustrated above between the two great classes of words it is necessary to deal briefly with the question, how do words obtain their meanings ? or, as it may be otherwise put, how do things of all sorts, mental and physical, obtain their names ? and to inquire to what extent the process differs in the two cases

[1] Steph., 298. [2] *Ibid.*, 97. [3] *Ibid.*, 154.

respectively. Let us ask, first, how is the identity of the subject of discourse determined as between two interlocutors in the case of any common outward object? secondly, how is it determined in the case, say, of a mental emotion? or, to put the question thus, when you or I are speaking about a pen or a pencil, how do we know that it is the same thing that we are speaking about? and again, when we are discussing the nature of the emotion, Hope, what is it that gives us the same certainty in that case?

The answer in the first case seems a very simple matter, but it less simple than it seems. Familiarity, indeed, it has been well said, is often the thickest of all veils. That which ultimately determines the identity of the outward object as between two interlocutors, lies in the fact that it is not possible for one of them to lay his finger on the same part of the same object as that on which the other has laid his finger without displacing it. 'This fact,' to quote my article in *Mind* already referred to, 'is the foundation of the distinction between the primary and the secondary qualities of matter. It is that which subsequently becomes elaborated into the thought that two bodies cannot occupy the same space at the same time. On it is based the very possibility of the denotation of words, of the pointing out of anything. The ultimate meaning of the words, "the same thing," as between you and me, is "the thing that I now lay my finger on, and that you cannot lay yours on without displacing mine. If you could, your finger would occupy the same space that mine occupies at the same time. As vision is a compound of muscular and colour sensations, it holds, in respect of this peculiarity, an intermediate position. I can see a face without displacing you, but not a face strictly in profile while you see it strictly in profile also. As a result of this, pointing out, as a means of indicating, comes to be substituted for touching." We see thus that the conceptions both of the reality and identity of outward objects are given us ultimately by the sensations of touch and motor activity. Another interesting conclusion that emerges from our analysis of the situation is this; that it takes the intercourse of two persons to gener-

ate either concept. In absolute solitude, apparently neither would ever have emerged.

Contrast with the above the manner in which the emotion, Hope, must have obtained its name. How did men ever come to be certain that, in speaking about Hope, they were speaking about the same thing? I cannot point out to you the emotion to which the word refers. The utmost I can do is to narrate certain circumstances, say, the sight of a sail by a shipwrecked sailor, and tell you that Hope is the emotion that, in such circumstances, springs up. We are thus absolutely dependent here on the use of words themselves to identify for us the subject of discourse. In a case like this, as Professor Stout says, it is the word itself that objectifies the thought.[1]

From the profound difference in the modes of the assignment of meanings to physical and to psychological terms, very numerous and very important subsidiary differences arise, affecting the whole subject matter of the mental and the physical sciences respectively, differences which have surely been inadequately appreciated by the class of philosophers who attempt to illustrate mental, or what are the same thing, economic phenomena by geometrical diagrams. A distinction between the two classes of words which may intimately concern us at present lies in the fact that it is in the sciences of the outward world only that the isolated individual object with a name attached to it, can exist. The names of psychological phenomena are all class names, and the same is true of economic phenomena. To quote from another article of my own in *Mind*,[2] 'Technical nomenclature and technical meanings have no place in psychology. We have absolutely no means of affixing them to its phenomena. For the naming of what is physically indicatable, one pointing out is enough. The name can be at once affixed. What is not thus indicatable can only obtain a name as the result of many, perhaps of innumerable repetitions; and of the seizure by the thought

[1] *Mind*, O.S., vol. xvi. No. 62, p. 188. Cf. Breal's *Semantics*, Eng. trans., p. 243.

[2] April 1896, pp. 243, 244.

of the community of the common element in such repetitions. The name of every psychological phenomenon, in fact, registers the discovery of a law of nature as truly as the word 'gravitation' registers Newton's great generalisation. It thus becomes comprehensible how, by diving into the meanings of words, important and valuable truth is to be elicited. What we are really diving into is the stored-up experience of the race.' . . . . There is all the difference in the world between a question of language and a question of nomenclature. The "occasional meanings" of words are themselves a natural phenomenon, an evolutionary product; and the task of ascertaining the natural laws that give the rationale of these meanings, and explain the connection between them, must be the task of some science. Let any one set himself to endeavour to find a hypothesis that will give the rationale of the distinction between wit and humour, and he will find himself engaged on one of the problems of empirical psychology. Let him endeavour to explain and account for the various meanings of Identity, Reality, or Causation, and he will be at once deep in the problems of metaphysics. It seems, then, that the real task of the subject sciences is to explain and account for the meanings of such words, and that the meanings themselves are our data, which it is altogether illegitimate for us to twist or turn in any way.' [1]

Objection 2nd. Are the Questions of Economic Theory mere Questions of Words?—The above line of reasoning, though advanced primarily in connection with the objection to the validity of the appeal to the common use based on the alleged ambiguity of popular language, bears also on a second objection which it will be well to consider here, the objection that the validity of the appeal would reduce the

[1] *Mind*, April 1896, pp. 243, 244. Mr. F. B. Hawley, the American economist already quoted, expresses with force and insight, more or less similar views to the above in regard to natural language. 'There is no more reliable thread,' he remarks, 'to serve as a guide through the labyrinth of economic discussion than a comparison of any apparent result with the corresponding idea underlying popular conceptions. There is surely something intuitive in the unconscious cerebration of the race' (*Quarterly Journal of Economics*, vol. xv. p. 82).

questions of economic theory to mere questions of words. It is indeed sometimes suggested by the economists themselves that they are so. That suggestion is made, for example, by Professor Fisher in the course of the controversy above referred to.[1] We can satisfy ourselves, however, on a moment's reflection that that cannot be the case.

One of the questions of economic theory that we have had occasion to refer to, the question whether value, and consequently whether wealth, which is the sum of values, does, or does not, owe its existence to labour alone, is one that, at the present moment, divides every European legislature into hostile sections.

The doctrine of the Appreciation of Gold, again, which formed the basis of Bimetallism, was due, as I have endeavoured to show elsewhere,[2] to a confusion of thought between the abstract and the concrete, and was thus an error of theory pure and simple.[3] Among the practical results of that illusory teaching, however, was the policy that kept the mints of our Indian Empire open for twenty years after they should have been closed, thus making India maintain the price of silver, an import, against itself, and involving it in financial loss that certainly surpassed some of the great war indemnities of recent years.[4]

In very recent controversies a misconception in regard to the meaning of the word Value has played quite a striking part. The moderate men in the ministry have endeavoured to solace themselves and their public with the reflection that there can be no confiscation in cutting down the future

[1] *Quarterly Journal of Economics*, vol. xviii. p. 389.

[2] *Evolution of Modern Money*, pp. 311-13.

[3] The confusion was between a rise or a fall, say, of wheat in general, and a rise or a fall in any given cargo during the time intervening between the date of its harvesting and that of its final sale.

[4] In a paper read before the Economic Section of the Glasgow Philosophical Society (*Proceedings*, 1897-8), I made a rough estimate of this loss at £31,000,000. Germany gained a great part of what India lost. We provided her with an excellent market for the thalers that she had to get rid of. Sir David Barbour, I notice, recently calculates that the gain to the Government in the matter of exchange since the mints were closed, amounts possibly to seventy or eighty millions sterling. (See *Times*, 15th June 1911.) The quantitative economics has shown itself in that instance an expensive luxury.

value of the property of any landowner, so long as the present value is left untouched. But, as the value in any case means the money that a piece of land *will* fetch, it becomes plain that this attempted distinction between present and future value is an impossible one. If it is 'confiscation,' as Sir Edward Grey expressed it, to trench upon the present value, then it cannot be anything else than confiscation to trench upon the future value, with which the present value is quite inseparably bound up.

The truth is, that this idea of the merely verbal character of the questions raised in the discussions of economic theory rests on a confusion between the principles that apply to the assignment of names in physics, and those applicable in the subject sciences. Plato put the question, as we have seen: Is there such a thing as rightness or wrongness in the assignment of names? We can now see that the answer is that, as regards the class of things which can have their identity fixed by pointing them out, there can be neither a right nor a wrong; with regard to the sort of things that cannot be pointed out, the case is altogether different. If the Parisians, in a fit of penitence, were to re-christen their Boulevard Voltaire 'the Boulevard St. Louis,' no one could say that the new name was either more or less correct than the old. This thought of re-christening, indeed, brings home to us vividly the essential difference between the two classes of words. Anything that can be held in the hand, or pointed out, can be re-christened without the smallest difficulty. We have re-christened, for instance, the shift as the chemise, the stays as the corset, and the bustle as the dress improver. It needs only sufficient authority in the matter of costume to go on with such re-christening to any extent. But let any one conceive the idea of re-christening a psychological phenomenon, say, the emotion of Hope, and he will find himself altogether at a loss to know how even to begin.

He cannot hold Hope in his hand and point it out, and say, 'I propose that, in the future, we shall call this thing X.' The utmost that he can do would be to say, 'I propose that the emotion which, in the past, we have called Hope,

we shall in future call X.' But, as every one would always require to keep the old name before his mind when attempting to assign the new one, the essay at re-christening would be reduced to an absurdity.

Precisely the same thing applies to economic phenomena. We should be just as powerless to re-christen Wages as we would be to re-christen Hope. But, cannot wages be pointed out, just as gold can be? it may be asked. They can, in a sense, but with an all-important difference. I can lay my finger on a piece of the yellow metal, and say, 'This is gold.' That is enough. But if I see a pile of notes or sovereigns in front of me, I cannot say, 'This is wages, this is rent, or this is capital,' until some one gives me a history of the money, or lets me know its destination; tells me, that is to say, how it was obtained, or what is to be done with it. Wages, like Hope, is a word which is dependent on the use of other words for the identification, as between two interlocutors, of the thing which it signifies.

Jevons talked, indeed, of substituting the expression 'ratio of exchange' for the word Value, but he never got the length even of using that phrase himself precisely where 'value' would naturally have come into his sentence, much less did he succeed in persuading other people to do it. Professor Marshall endeavoured to re-christen the saving that a man makes when he gets anything for sixpence, for which he would have given a shilling rather than have gone without it as Consumer's Rent. But he had from the first that peculiar use of the expression practically all to himself, and even he, in the end, found it advisable so to modify it as practically to discard it.

The Consequence-carrying Character of Economic Names.—Suppose the question arises whether we shall call a certain planet Le Verrier, Adams, or Neptune, and we decide on Neptune, the matter ends there; no consequences whatever follow. Suppose, on the contrary, that you are in doubt whether to call a certain description of business gain 'rent,' or 'profit,' and you decide on 'rent,' the case is different. To call a particular gain rent, indeed, is, in the

view of the Ricardian economists, to say that you may confiscate it by taxation without harassing any one but the actual owner of the property rented.

In this case, thus, in bestowing the name, you are making a far-reaching assertion with regard to the nature of the thing on which you bestow it. You are committing yourself to predictions in regard to events that stretch away into the almost endless future, and if the name is a wrong one, the predictions, whatever they are, cannot fail to be wrong also.

We see thus how different a matter is the bestowal of a name on an economic universal, and the bestowal of a name on a concrete individual, or a physical species. The fact that economic naming can carry consequences has its origin in a circumstance relating to our modes of thinking that has not been sufficiently observed, if it has been observed at all, the fact, namely, that we are continually making assertions about the future couched in forms of language that seem to apply only to the present. Who would think, at first sight, that the simple verb ' to see ' has of necessity a future content ? Yet, as Berkeley acutely remarks, we are always in truth ' foreseeing.' We look some little distance into the future whenever, on glancing down the street, we say to ourselves that one of two houses in the distance is only half as far from us as another. The real meaning of our thought is that it *will* take us only half as long, and will need only half as much effort to reach the first as it will to reach the second. If, as he remarks, a seeing man should appear suddenly among a race of blind men, his power of foreseeing danger, in the shape of precipices and the like, would undoubtedly seem to them altogether miraculous.

Mill endeavours to fortify his determinist position by arguing that if we knew a man's character perfectly, we should know what he would do in any given circumstances. Of course we should ; but what Mill fails to notice is, that the words ' to know a man's character perfectly ' mean just this, and nothing else : ' To know with precision what he would do in any given circumstances.' The future is

expressed in words that apparently belong to the present only. Similarly, the mathematical economists speak lightly of hypothetical communities in which a perfect knowledge of market conditions exists,[1] unconscious apparently of the fact that such knowledge would imply miraculous foreknowledge of the whole endless future in regard to these markets.

Why is it that we are thus always predicting the future, yet always imagining that we are concerned only with the present? This is assuredly a psychological question of great interest and suggestiveness, and one well worthy of ampler investigation than can be accorded to it here. We know, indeed, that our nouns of all sorts are framed on the model of the isolated outward object,[2] with its rigid boundaries in space, the very type of existence in the present; although such nouns even as a 'journey,' much more such nouns as a 'constitution,' have very little true affinity with such a type. There is such a thing, it seems, in our thinking as reification as well as personification; and it is in connection with that singular fact of our mental processes that we have to look for the solution of the problem. Even abstract attributes of things such as their value, as we have seen in our reference to Sir Edward Grey's reasoning in regard to the new land taxes, come under the influence of the reifying tendency. We think of value continually as something that exists in the present while we know, on reflection, that the whole content of the concept pertains in truth to the future. The element of futurity in the nature of wealth will be found worth reverting to later on.

Objection 3rd.—A third objection to the validity of our principle of the appeal to the common use, takes the shape of the contention that its concession would postulate the rigidity of language. Its detailed consideration will occupy our attention in the following chapter.

[1] Marshall, *loc, cit.*, p. 334. He speaks of 'every dealer who has a perfect knowledge of the circumstances of the market,' that is, who knows the whole future. Cf. also p. 497.

[2] Lotze, *Logic*, Eng. trans., book I. chap. i.

CHAPTER IV

THE PRIMARY MEANINGS AND THEIR EXTENSIONS

We have, as was observed at the close of the last chapter, to examine, in the present one, a third objection to the appeal to common use in language, as decisive in regard to the questions of economic theory. It is to the effect that the admission of such an appeal would imply a belief in the rigidity of language. Now it must, of course, at once be admitted that such a belief cannot for a moment be entertained. Nothing is more certain than this, that language is instinct every moment with the spirit of life, development, and change. If that is so, however, how, it may be asked, can common usage be viewed even as a possible criterion of what is valid and permissible in respect to it.

In this connection a passage from Sir Henry Maine's *Ancient Law* suggests itself. It is primarily applicable, no doubt, to jurisprudence, but has, at the same time, a fairly obvious application of a more general character. 'When a group of facts,' he says, 'come before an English court for adjudication, the whole course of discussion between the judge and the advocates assumes that no question can be raised which will call for the application of any principles but old ones, or of any distinctions but such as have long since been allowed. . . . Yet the moment the judgment has been rendered or reported, we slide unconsciously or unavowedly into a new language and a new train of thought. We now admit that the new decision has modified the law.' We seem to see here, as regards jurisprudence at any rate, the possibility of reconciling the appeal to precedent in language with the recognition of its continual tendency to change and development.

We have, in the first place, to distinguish clearly between the principles that are applicable to the primary meanings

of words and those that are applicable to their extensions. The expression the 'primary meaning' is borrowed from the writers on the interpretation of statutes and contracts. In regard to such interpretation the law has no principles that are recondite or technical. Everything, on the contrary, is in perfect accord with the ordinary common sense of the average man. 'In the construction of a contract,' says Hardcastle,[1] 'there cannot be said to be any rule of law applicable, but the governing principle is to ascertain the interests of the parties through the words they have used, which words are to be taken in the sense which the common usage of mankind has applied to them in reference to the context in which they are found.' The primary meaning is thus, as Sir Howard Elphinstone remarks, 'not the etymological or dictionary meaning,' but rather the meaning determined by common use, taking the context and all the circumstances of the case into account.

What, then, as to the extensions? I cannot better illustrate their nature than by reverting briefly to an example taken from jurisprudence, cited at greater length in one of my former books.[2] The case referred to was that of Powell *v.* the Kempton Park Race Course Co., and the circumstances were as follows:—An Act had been passed in 1853 for the suppression of betting-houses. Towards the end of last century it came to be thought in some quarters that possibly the Act might be made available for bringing to an end the operations of bookmakers on the race-courses. In the course of one of the cases raised with that object in view, Lord Coleridge remarked that if a bookmaker stationed himself under an umbrella fixed in the ground in the enclosure by the grand stand, he would certainly be using a betting-house. The bookmakers took the hint, and in the future avoided stationing themselves under umbrellas. The question, however, then arose whether the very enclosures themselves were not, in all the circumstances of the case, betting-houses. Mr. Justice Hawkins decided that they were, and it was in order to get this decision

[1] *Statutory Law*, p. 7.

[2] *Economic Method and Economic Fallacies*, chap. iii.

reversed that the case above mentioned was brought before the House of Lords. In the end, it was decided in a sense adverse to this view, though not without dissent on the part of two very eminent judges, Lords Davey and Hobhouse. Among the deliverances by various members of the Court was one of some interest for our present purpose by Lord James of Hereford. The Act, he remarked, was certainly not intended to put down betting everywhere, the prohibited betting-house could not be interpreted as being a man's private house or club. The Act could not, moreover, apply to a large area like Salisbury Plain, neither could it, in his view, apply to the enclosures used, no doubt, on the payment of an entrance fee by the bookmakers and their customers, but also by great numbers of people who did not bet at all.

The ' primary meaning ' in such a case would be a betting-house established, say, in Oxford Street, W. We have seen this meaning in process of extension first to the fixed umbrella under which the bookmaker stationed himself in the enclosure by the grand stand ; secondly, to those enclosures themselves. Here, however, the word entered a sort of neutral zone lying between what was clearly a betting-house and what was not, a zone in which the most competent of tribunals might be divided in its verdict as to the meaning that could rightly be assigned to the expression. All our words, unless indeed they are the names of individual things, are subject to similar extensions. Mill remarks of the word ' acid,' for example, that ' as experimental discovery advanced, the substances classed with acids have been constantly multiplying, and by a natural consequence the attributes connoted by the word have receded and become fewer,' and thus ' acid ' now means merely that which will redden vegetable blues, if even this characteristic is to-day essential. ' Metal,' we might think, has a definite enough meaning, till we are faced by the question, Is hydrogen a metal ? or, What are we to say of radium and helium ? The definiteness and precision that we attach to mathematical conceptions do not prevent them from running a similar course. ' The equation of

the ellipse,' says Lotze, '$a^2y^2+b^2x^2=a^2b^2$ leaves the two axes, a and b, to be chosen at pleasure, and the formula claims that it will always produce an ellipse whatever values we may assume for a and b, and therefore if one of them be assumed to=0. But in that case the curve passes into a straight line, and the result which this value gives falls accordingly under the concept N, that of the straight line which is different from that of the ellipse.' [1] Changes in degree thus in the determining characters of the ellipse, if carried far enough, can take it out of its original genus and bring it under the formative law of another genus altogether, just as the accumulation of almost insensible changes in the meaning of the word betting-house could take it, in the view of the majority of the Court, out of the class of things to which the Act of 1853 was intended to apply, and could bring it into another class altogether, that to which the Act could not apply.

To turn to economics for one or two examples, we have seen how M'Culloch, by dropping one limiting characteristic of the concept of labour—its connection with mankind—widens it to such a degree that the word becomes really nothing more than a synonym for causation in its most general sense. In a similar manner, the very definite economic term 'price' has had, in Professor Marshall's hands, its meaning so whittled away by successive extensions of its application, that practically none whatever is left in it. The crop that an acre of land yields is said to be the price that the land pays for the labour and outlay.[2] This, of course, at once divorces the thought of 'price' from its connection with mankind, precisely as M'Culloch's theory effects a similar divorce with regard to the thought of 'labour.' You put in a row of cabbage plants. The adult vegetables are the price that you receive for your trouble. That is poetry, however, rather than science. But, again, suppose that, instead of putting in a row of cabbage plants, you put in an acorn. Who gets the 'price' now, whatever it may be conceived of as being? Someone, perhaps, who walks the earth long after your very

[1] *Logic*, Eng. trans., vol. i. p. 172. [2] *Principles*, 5th ed., p. 157.

name has been forgotten. There is then further an absolute divorce effected between the doer of the act and the receiver of the reward ; and Professor Marshall's application of the conception of the supply price of labour to the wages that a given generation of men can expect to command owing to the exertions and sacrifices of a previous one,[1] illustrates this second divorce conspicuously enough. When we find, further, the effort made to contemplate the fact of the success of one form of business organisation in supplanting another [2]—say, of the larger in supplanting the smaller—as the supply price of the first, one cannot help feeling that we might just as well be told that the prey of the lion is the supply price of its teeth and its claws, or the immunity from innumerable dangers to which the bird attains is the supply price of its wings. Success in the struggle for existence, and not price of any sort, is surely the category under which in both cases the conception naturally falls.

A description of illegitimate extension which seems to present an invincible attraction to many economists is the extension of the literal meaning of facts and things to their causes, absorbing the two, the cause and the effect, under one over-generalised conception. Cause and effect certainly sometimes approach each other very closely in meaning. It seems hardly to be passing the bounds of what is permissible for example, to reckon the skill of the Lancashire cotton-spinners as a part of our national wealth, instead of regarding it simply as one of its causes. Still, this is the sort of extension that may land us, before we are aware of it, as in the case of the ellipse, within the sphere of another concept altogether. By permitting himself just a little of such latitude, a German investigator [3] arrives at the conclusion that God Himself might not unreasonably be reckoned as capital 'if it were not improper to include the Eternal under a transitory economic category.'

We must, it is clear, thus sharply distinguish the primary meaning, the meaning of the typical instance, or the typical object, from which we learn originally the denotation of the

[1] *Principles*, p. 340. [2] *Ibid.*, pp. 313, 605.
[3] Walcker, quoted in Robertson's *Fallacy of Saving*, p. 65.

word from these extended meanings. When we do this, we can see how it is that the fact that there is one sphere of word meanings in which all is, or should be, recognised as perfectly definite and certain, is not necessarily inconsistent with the existence of another sphere where change and development are admissible. In jurisprudence such definition and certainty as regards the primary meanings is of course well established. In that branch of thought no one ever so much as dreams of calling their validity in question. It is inconceivable indeed that any one ever should. If a man is charged with breaking into my house at night, and going off with the contents of my safe, no question can be raised as to whether the act imputed to him is burglary or not. It is the very type of burglary. The arguments of the lawyers on both sides will bear only on the question of fact, on the evidence brought to sustain the charge.

Negations of the Type in Philosophy.—When we turn to abstract philosophy, however, a strange phenomenon presents itself. In that sphere, instead of our finding that the primary meanings of the salient terms of our subject-matter are looked on as sacrosanct and indefeasible, we find, on the contrary, that it is around these very primary meanings that the great and spirit-stirring controversies of modern philosophy have raged and still rage.

Take the word Real, for example. How have we learned its meaning ? Plainly from having had the rocks and trees, the chairs and the tables, and so on, of the outward world pointed out to us, and being told that these and such things as these are real, or, it may be, still more probably from having picked up this information unconsciously from those about us. We entertain no sort of doubt, at any rate to begin with, that such things are real. The Humist, however, comes along and raises a question on that very point. We do not turn away from him with a smile ; on the contrary, we are profoundly impressed, and literature is enriched with innumerable volumes devoted to the discussion of the question of idealism *versus* realism in its manifold aspects.

Let us suppose, however, that we have to deal with some less abstract conception than that of reality, we will find that we deal with it in quite a different fashion. Take the conceptions of animalhood and planthood for example. When we designate one organism an animal, and another a plant, we must, it is clear, in the first instance, have some type of the animal and the plant to predicate by. We find the first, say, in the dog, the second in the cabbage. We are clear thenceforward as to the animalhood or planthood of other things in nature in proportion as they resemble the dog or the cabbage in essentials. When we reach the micro-organisms, the experience and acuteness of a Darwin or a Huxley may be needed to tell us whether any given individual among them is to be ranked with the animals or the plants. There we reach the sphere of the extended meanings, and there, consequently, doubts and difficulties enter. As to the type instances themselves, the dog and the cabbage, it has not yet occurred to any philosopher to raise a question as to their claim to animalhood or planthood. No one, up to the present, has suggested that there can be anything more truly vegetable than a cabbage, or more truly canine than a terrier. We accord to the less abstract type thus an entirely different sort of treatment from that which we accord to the more abstract.

Negations of the Type in Economics.—Whatever may be the justification of the method of procedure which admits of the negation of the type in metaphysics, it will probably be generally admitted that economics should follow the principles that rule in jurisprudence rather than those that seem to rule in the more abstract science. No doubt the questions raised in regard to economic language apply frequently only to the extended meanings; still, however, we have seen that there are economists in abundance who claim in practice the right to call the typical meaning itself in question. This is done, for instance, by Mr. George—and accepted, I imagine, by his large following—when he tells us that the payment of wages in production never even temporarily diminishes capital. It is done by Professor

von Boehm Bawerk, when he calls in question the validity of the statement that interest is payment for the use of capital, and by such writers as Mr. Macfarlane when they inform us that they employ the terms 'rent,' 'profit,' 'interest,' and 'gain' in senses entirely different from those sanctioned by common usage. If the principle for which we have been contending is valid, then all such contentions would be traversed at once and finally by the *reductio ad absurdum*. If it is not valid, then indeed we must ask, can any conclusion be definitely established in the whole region of economic theory, or is speculative thought there a vessel at sea without a compass.

Proof in Economic Theory.—I should reckon it no small achievement if I could convince any reader, hitherto unconvinced, that definite proof even with regard to the plainest conceivable proposition of economic theory is possible, say negative proof in regard to Mr. George's proposition that 'wages are never paid out of capital.' Reliance on similar proof in more complicated cases would assuredly follow. It is noteworthy how seldom one finds any economist who is alive to the fact that proof has any sort of possible application in this region. Professor Pigou, to his credit, is an exception. At the same time the examples of proof with which he furnishes us are eccentric rather than convincing. He has occasion to remark that 'Fluctuations in the income of a poor man cause more disenjoyment . . . than fluctuations in that of a rich man of similar temperament.'[1] He appends a note to this effect. 'The proof of this proposition is as follows:—When a man gets $(n-1)$ shillings to-day, and $(n-1)$ shillings to-morrow, instead of getting n shillings each day, there is a loss of utility, other things being equal, measured by the difference in utility to him between the nth and the $(n-1)$th shilling,' and so on through a quarter of a page of algebra, ending with the assertion that '$\frac{d_3U}{dx^3}$ is negative.' Now, this may be an accurate enough translation of the above statement

[1] *Industrial Peace*, p. 70.

into the algebraic notation, for all that I know, but as to its being a proof, it is obvious that it is no more a proof than a translation of it into French would be. Professor Pigou, indeed, himself ends off with the observation that 'once this proposition is clearly stated, it commends itself to common sense.' That is true, and in that fact plainly lies its one and its only proof. Every 'why' rests ultimately on a 'that,' and we are driven to fall back on self-evidence, on the *reductio ad absurdum* of the contrary, in the long-run. If you take any common universally accepted statement about the things of the outward world, say, the statement that liquids when moved retain their size but not their shape, you find on reflection that it may be divided into two separate assertions; one to the effect that certain substances when moved retain their size but not their shape; the other, that these substances are named 'liquids.' The proof of the first lies in the province of observation and experiment. Our treatises on Logic deal with it extensively, and with it alone. How is the truth of the second proposition proved? We say that it is self-evident, in other words, we appeal to common usage in language to validate it. Our principle thus is not very different from the famous doctrine of Descartes that the ultimate criterion of truth in philosophy is 'the evident conception of a healthy mind so clear and distinct that no doubt is left.'

The impression is a common one, no doubt, as the history of metaphysical speculation shows, that there is something less cogent in the self-evident proposition than in the proposition that rests on a chain of reasoning. We do not, however, apply this view universally. No one, for example, thinks that the fourth proposition of Euclid, which rests on self-evidence, is less cogent than all the elaborate proofs of the other propositions that are based upon it.

So much, then, as to proof in economics, or rather, we should say, in economic theory, so far as the primary meanings of words are concerned. As regards the manner in which the appeal to the common use can be applied in

reference to the extended meanings, much is to be gathered from the discussions on the point of law such as that of which an instance has been given. We have only to reflect on the nature of predication itself to understand how inevitable must be the tendency towards the continual extension of the meaning of words. Predication consists ultimately in the likening of the unknown, or the half known to the well known. Given one thing, *A*, that you and I both know, such as the wave motion caused by a stone thrown into a pond, I can convey to you information more or less perfect about a second thing, *B*, say the sound waves in the atmosphere, by telling you that it resembles *A*, and, in the long-run, it will be found that I can convey it in no other manner. Developed language may disguise the fact, but it cannot alter it. There is thus always a tendency at work impelling us to hunt for previously unnoticed similarities in things, propositions, or events in order that, by means of them, we may convey information to our neighbours; and thus the spheres of our concepts are always widening out from their centres. One result of this is that the sphere of each concept is continually liable to approach, and perhaps to cross, the boundary that separates it, or should separate it, from the sphere of another concept, and we have to be continually on our guard that, in our use of words, this should not take place.

It is obvious, too, that there is a natural order in these extensions which it is right and reasonable to follow. It may be legitimate, and for some purposes, necessary, to admit the validity of the application of the word 'rent' to cases in which there is neither a tenant nor a landlord, but where the tenant-landlord is supposed, by a legal fiction, to pay the rent to himself, but it is manifestly improper to treat this legal fiction meaning as the primary one, or as the only true and scientific one. Yet this is done even by so reasonable and untechnical an economist as Cairnes, and, of course, the principle of treating the legal fiction meanings as the scientific ones is followed universally by writers of the Austrian and mathematical schools. The economist who always conceives of rent as legal fiction rent, is supposed

to occupy a higher plane of thought than those who, with the common herd, regard it as emerging out of the relation between landlord and tenant.

In M. Michel Bréal's *Semantics*,[1] the importance that should be attached to popular conceptions is dwelt upon with much emphasis. 'The distinctions that are made by the people,' he says, 'are the only true and the only good ones.'[2] The following, too, is interesting and illuminating. 'Littré's *Dictionary* gives no less than twelve columns to the word *à* alone. Yet the people finds its way with no difficulty in the seeming chaos, not, as we have seen, owing to a more or less clear notion of the import of the word: no more than the philosophers would it be able to give a definition that fitted every usage. It allows itself to be directed to a certain number of expressions which the memory retains, and it uses as models.'[3]

We have here a glimpse of the philosophical basis of our contention. The right use of a word in living speech is plainly possible where its definition is plainly impossible, just as one may be able to strum a tune on the piano without knowing anything about the theory of music, and this right use, therefore, can be appealed to, to correct or to confirm a philosophical definition.

There is this great difference between the fresh use of a word that naturally arises, and then becomes general, and the new technical expression that some theorist invents and attempts to force on public acceptance. The first is the creation not of one mind alone, but of the first utterer, in conjunction with those who listen to him. Unless the new term, or the new meaning given to an old term, catches on, it is dead; the second is the mere arbitrary creation of one individual. In that fact lies the advantage which the popular distinction possesses over the theoretical one. The first comes to us already accepted and established; the second does not. If the popular distinctions, however, are alone true and alone good, then phraseology which is

[1] Translated by the Hon. Mrs. Cust.

[2] Eng. trans., p. 28.

[3] Littré's *Dictionary*, p. 242.

not based on any popular distinction must be looked on as suspect from the beginning, or, indeed, as out of court at once. The acceptance of the principle would soon prove fatal to a continuance of the elaborate affectation, so prevalent at present among the economists, of dealing with pecuniary concepts in non-pecuniary terms.

CHAPTER V

THE MARGIN

THE reader who has taken the trouble to follow me thus far, will now have seen the principle of method at work for the validity of which I have been contending, and the observation of it at work should be calculated, I think, to remove some of the misunderstandings and difficulties which could hardly fail to present themselves on its first formulation. In economics, as in jurisprudence, there will always, no doubt, be cases in which it may be a difficult matter to say to which of two alternative uses of a term must be credited the characteristic of being that which is most closely in accord with the usage of living speech, but, for all that, if it were once generally admitted that accordance with usage is to be looked on as a necessary qualification of the valid employment of economic language, it ought then to be possible to rescue some considerable area of the science from the billows of perpetual controversy under which it is at present nearly or altogether submerged.

The alternative course is to concede to every economist the right that so many of them claim, that of using economic language in whatever sense they please, so long as they maintain their self-consistency in their use of it. If that claim must be conceded, then, indeed, General Walker's problem is insoluble, then there can be no such thing as either the right or the wrong use of any economic term ; all uses, on the contrary, must be held equally legitimate, and equally illegitimate. It must be said, however, that the economists who assume nominally this attitude in regard to language do not, in truth, take themselves quite seriously. They, for their own part, usually think it necessary to expend anything in the way of letterpress up to a volume,

and even more, in demonstrating that their own particular use of such words as 'Capital,' 'Value,' 'Rent,' and 'Profit,' is the right one; and the ground of their demonstration, when analysed, is generally found to be, in one shape or another, the appeal to common use.

If our principle, at any rate, has any sort of validity, it will be seen at once what an immense advantage, as media of investigation, the words that are in everyday use in the business of life must possess over the novel phraseology which economic theorists in recent years have lavishly introduced into the science, and which has certainly had an extraordinary measure of success in permeating the whole field of discussion. The phrase 'marginal utility,' for example, has, of course, as we know, no common and practical use whatever; no one employs it in any business communication, or in any other fashion indeed outside a text-book. Hence, when we find it used in the discussions of economic theory, it is not easy to see what means one can possibly have of ascertaining whether it is used rightly or wrongly. In its case there is no natural criterion whatever to appeal to.[1] To my mind, I confess this fact alone is quite sufficient to stamp it as an expression to be avoided, as at the best tiresome and useless, at the worst a source of erroneous thought. We will not, however, condemn it unheard. The present and the following chapters will be devoted to an examination on its own merits of the marginalist theory.

First Appearance of 'The Margin' in Economics.—The conception of the 'Margin' made its first appearance in economics in the formulation of Ricardo's law of rent. We then first began to hear of the marginal land which will return the costs of cultivation and yield normal profits to the farmer, but which will afford no surplus available for rent, and of the marginal doses of capital and labour applied to any land, in regard to which the same statements may be

[1] The same applies, of course, to the 'discommodities,' 'disutilities,' 'negative values,' 'quasi rents,' 'consumer's rents,' etc., and to Professor Marshall's 'supply price,' and 'demand price,' which do not correspond to what any one else would naturally mean by those expressions.

said to hold good. These earliest examples of the Margin have this much in common with all later ones, that one can expatiate on them, and can suspend chains of reasoning from them to his heart's content so long as he confines himself to the consideration of them in the abstract, but that when we come to close quarters with them, and ask the theorist to show us any actual piece of land that at this moment is marginal, or any specimen of work at present going on on any farm that involves just the marginal dose of expenditure, we find that no satisfaction is to be got out of him. Some writers, we find, are of opinion that we have to look for the marginal wheat land in the far west of the United States, or of Canada; others, on the contrary, think that it is to be found in Essex, or in Massachusetts. As to the marginal doses of expenditure, they are evidently something that it is still, if possible, more difficult to locate and to identify in individual cases than is the marginal land. Ask any farmer whose ploughing and harrowing operations you see in progress, whether he himself can point to any of the work that he has put in hand that will just cover expenses and normal profits, and no more. He will probably answer: 'I can enlighten you on that point if you will tell me what the coming season will be like, and what next year's prices for wheat will be. As things stand,' he may add, 'if the price of wheat is over thirty shillings a quarter, all the work that you see going on will most likely pay me well; if the price is down to twenty-five shillings, a good deal of it will be done at a dead loss.' It is clear indeed that, in order that it should be possible for us to lay our finger on any individual specimen of marginal land, or of marginal doses of expenditure, we should have to know, among other things, what next year's prices for produce will be. So long as this knowledge is out of our reach, so long will things marginal likewise be for us incognisable.

Consider, however, what is the nature of a general conception with regard to which no one can indicate any individual thing or fact that is embraced under it. This peculiarity, at any rate, it will be admitted, differentiates such conceptions from those that are expressed by the

universals of ordinary language. The latter are distilled from individual instances; the former plainly cannot be. They remind one of the empty cases in a museum with the labels on them, but with no specimens inside them. The new economics is full of these shadows. The popular use of language will have nothing to say to them.

Some of my readers, however, may answer: But if farming in one place is beyond question profitable, while in others it is known to be very much the reverse; and if we are justified in assuming that there exist in the world an endless series of gradations between these two conditions, then must there not be marginal land and marginal doses of expenditure to be found somewhere, if we knew where to look for them, and if so, may we not fix our attention on them, and make them the subjects of contemplation and discussion? By all means let us do so if we think it worth while, so long as we are careful to avoid the fallacy of taking them for what they are not. Let us remember that they are at the best mere 'must be's,' and that the very utmost that we can know about them is that they must exist somewhere. Do not let us glide into the habit of speaking about them as if they were things as familiar to us as St. Paul's Cathedral or Nelson's Monument. Some even of the most eminent of our economists have, I think, allowed themselves now and then to forget that there are things with regard to which it may with some confidence be asserted that they must exist somewhere, but which for all that are as far beyond our ken as if they were, like 'the gems of purest ray serene'—the must-be's of the poet—covered by countless fathoms of the unplumbed ocean.

Marshall's Margin of Immigration, etc.—It will serve perhaps to illustrate my meaning if we glance at some special instances of the use of the marginal concept. Here is one, for example, from Professor Marshall's *Principles of Economics*.[1] 'When a new country is first settled,' he remarks, 'and land is free, immigration proceeds up to the

[1] 5th edition, p. 429, sidenote.

margin at which the pioneer's endurance is just rewarded.' This point he calls 'the margin of immigration.' We hear similarly of a margin in agriculture, where the use of horse-power stops, and that of steam-power begins,[1] of one between the use of skilled and unskilled labour;[2] of the margin of building,[3] the point, that is, at which people cease to add more stories to their houses and build on fresh land instead; of the margin between the use of machinery and of labour,[4] between additions to the staff of foremen and that of ordinary workmen,[5] and of that between rival methods of business organisation, the large and the small.[6] The simplest, perhaps, of these is the first mentioned, 'the margin of immigration.' Referring to the statement in regard to it quoted above, suppose we were to ask the writer, 'How do you know all this, that when a new country is first settled and land is free, immigration proceeds up to the margin at which the pioneer's endurance is just rewarded?' his answer would necessarily be this, that there must be a point or zone somewhere which settlement has for the moment reached, and beyond which lies at present the unoccupied wilderness; and further, that if this point were not the point at which the pioneer's endurance was just rewarded, settlement would either have advanced farther, or would not have advanced so far. When all is said and done, therefore, the whole statement amounts merely to this, that settlement has advanced to the point to which it is found to have advanced, or more simply that settlement in the new country has taken place. Whenever, and wherever, settlement is in progress, all the rest of the statement holds good with reference to it. Its setting forth in words adds nothing whatever to the simple proposition, that settlement is in progress, or is taking place.

In real life would any one think of speaking about a margin in such circumstances? Of course there must always be some stage which development of any sort has, at a given moment, reached, and perhaps you may, if you please, call this stage 'the margin,' but language is ordin-

[1] *Principles of Economics*, 5th ed., p. 405. [2] *Ibid.*, p. 405.
[3] *Ibid.*, p 448. [4] *Ibid.*, p. 522. [5] *Ibid.*, p. 599. [6] *Ibid.*, p. 605.

arily used to communicate information, and such a use of it communicates none at all. Your audience, at the same time, are likely to assume that you do mean to communicate some information, and so the statement is not only surplusage but is also misleading. If your margin corresponds to any general rule, if 'the margin of immigration,' for example, was always to be found just ten miles from a railway station, then there would be some point and some significance in speaking about it. If it means merely the *de facto* stopping point, which neither you nor any one else can say anything about till after the event, then the mention of a margin does not appear to be legitimate. It means nothing at all. To refer to another example. We are told [1] that 'there are some kinds of field work for which horse-power is clearly more suitable than steam-power, and *vice versâ*.' In such circumstances the application of steam-power will be found to have been 'pushed just so far that any further use of it in the place of horse-power would bring no net advantage.' This is the margin between the profitable use of steam-power and horse-power. We are specially told, at the same time, in a note,[2] that 'the margin here will vary with local circumstances, as well as with the habits, inclinations, and resources of individual farmers.' Similarly with regard to the margin of profitableness between different methods of business organisation, it is said that it 'is to be regarded not as a point on any line, but a boundary line of irregular shape, cutting one after another every possible line of business organisation.' [3] That is to say, that it possesses no general characteristic that can be made the subject of communication between man and man. With regard to the margin of building, it is frankly owned that the top story can by no means be regarded as always the marginal part of the edifice in the sense of being the least profitable. The writer, however, adds that 'to fix the ideas,' [4] he will suppose that to be the case for the present. That certainly will not do. The remark, however, is noteworthy as indicating a perception on the part of the

[1] *Principles of Economics*, 5th ed., p. 405.
[2] *Ibid.*, p. 405.
[3] *Ibid.*, p. 605.
[4] *Ibid.*, p. 445.

writer that these margins need something that will 'fix the ideas' about them, and that, as presented, they have not got it.

If in economics, one is impelled to ask, these elusive phantasms have anything in them that it is either possible or desirable to convert into the subject of elaborate discussions, why then in economics alone? Wherever throughout the whole sphere of life any process of gradual change is in progress, you can conjure up a 'margin' quite as easily as in economics. The black-haired and black-eyed people of Europe, for example, are at present steadily supplanting the fair-haired and blue-eyed. Why does no one dilate on the margin of expansion reached by the former, and tell us that it is now being 'pushed outwards'? The reason, I imagine, is that every one knows that by saying this he would add nothing to the statement that the one is supplanting the other. He would merely be raising a cloud of words to vex the souls of the uninitiated. We are told that we should study economic changes, say, the change from horse-power to steam-power 'at the margin.' How could we conceivably study them anywhere else. The margin is merely the point or waving line where the change is taking place. We might as well be told that we should always study history with a reference to the past, or that in studying geography we should never fail to keep spatial conditions in view. In the process of 'unconscious selection' that Darwin has occasion to refer to, by which the laying capacities of hens have been improved, why does he not think it necessary to dwell on the margin between the hens that go to the pot in early youth, and those that are left to multiply and replenish the farmyard? There is undoubtedly a marginal zone somewhere between the two classes, just as truly as there is one between the use of horse-power and steam-power, or between the expansion of the large and of the small forms of business organisation. In the interests of our present line of study, it is indeed much to be desired that attention should be turned to some of the innumerable margins that are to be found in natural science, in history, in theology even, and that the hard-

driven margins of economics should be allowed a period of repose.

We find then, to summarise the conclusions that have so far emerged, that the margin of the theorists is (1) a deduction from the context; (2) that, being in the context already, statements in reference to it convey no fresh information; (3) that a suspicion that this is so is discoverable in the expressions of the theorists themselves. Fresh characterisations consequently of the margin that are admittedly untenable, have to be introduced in order, as it is said, 'to fix the ideas.' In addition to the above conclusions, there is one other that remains to be noted. That is this: that the concept of the margin is based always or nearly always, on the confusion between a fixed point and an average. As regards the marginal dose of labour, it was conceded in passing for argument's sake, that it must exist somewhere, but even this is by no means certain. Seven and a half is the average of five and ten, but, in the real world, in any given case, there may be only fives and tens, and no seven and a halfs. So there may be endless doses of capital and labour that do more than cover costs and normal profits, and endless doses that do less, but none for all that, in which the coincidence between costs and profits is exact. The 'margin,' thus, in such cases is not only incognisable, but maybe non-existent.

The Margin as applied to the Labour Question.—There is one application of the marginal theory that has brought it into contact with an issue that is very much alive indeed, that, viz., of the equitableness of the remuneration of labour in the modern civilised world. This circumstance has gained for it a fairly wide celebrity. We find the theory, indeed, erected into a sort of theodicy, a justification of the ways of God to man. In Professor Clark's view,[1] nothing less than the right of society to exist in its present form depends on the establishment of its validity. The special setting of it which is most familiar, is that of Professor Marshall. The whole doctrine, however, and even

[1] *Distribution of Wealth*, p. 3.

the illustrations that accompany it, are adaptations from Von Thünen, a German economist, who flourished in the earlier part of the nineteenth century, whose 'brilliant researches' are spoken of in very warm language by Professor Marshall.[1]

The Marginal Shepherd.—Von Thünen arrives at the conclusion that the value of the work of the last hired labourer constitutes at the same time his wages.[2] This is probably the first application of the marginal concept as the basis of a theory of wages or prices of any sort, and is thus the germ of a literature that is now enormous in volume if not in value.[3] Professor Marshall adopts this conclusion, and to popularise it, makes use of his well-known illustration of the hiring of the marginal shepherd.[4] A sheep farmer, he says, may be in doubt as to whether his staff of shepherds is sufficient. He may come to the conclusion that if he hired an additional man, so many more lambs would be kept alive that he might expect to send to market twenty more sheep every year. 'Then,' as he remarks, 'the net product of that shepherd's labour will be twenty sheep: if the farmer can hire him for ever so little less than the price of twenty sheep,[5] he will decide to do so, otherwise not. The shepherd who is on the margin of not being employed—the marginal shepherd, as we may call him—adds to the total produce a net value just equal to his own wages,' and thus, it is argued, the labourer gets just what he produces.

The Isolated Case Fallacy.—Now, of course, it might happen that, in a given case, as a matter of fact, the last

[1] Some, however, of Von Thünen's mathematics are too indigestible even for the most robust of modern organs. To find the natural wage, for example, he tells us, we must multiply the indispensable needs of the labourer by the product of his work, and *extract the square root*! (*Der Isolirte Staat*, vol. ii. part i. p. 15.)

[2] *Ibid.*, p. 19.

[3] See E. von Boehm Bawerk, *Capital and Interest*, vol. ii. book III. chap. ii. sec. 1, note to p. 224.

[4] Von Thünen's more or less parallel illustration is that of a labourer hired to dig potatoes.

[5] Next year's price, and that of succeeding years!

shepherd put on might save alive twenty sheep, and that the value of the twenty sheep might be found, after the event, to be about equal to the wages paid him, but we must take care not to confuse the individual case and the retrospective point of view with the case of generalised experience, which can be used as a basis of prediction and of consequent action. It is safe to say that the sheep farmer is not born yet who would, or could, think out the question of putting on an extra shepherd in the manner here represented. No one could, of course, say, with even the roughest approximation to probability, how many sheep an extra shepherd would save. In some conditions of the seasons, say, in the case of a flood, he might save hundreds, in others none at all; nor could any one know what next year's prices of sheep would be. But our sheep farmer would have to be informed on both these points before it would become possible for him to make the precise calculation suggested, ending in the decision that he would take the man on if he could get him for 'ever so little less' than the value of the sheep that he would save.

By this line of reasoning, the marginal net product of labour is put forward as if it were something that had an independent existence cognisable to any one, something, consequently, that could be set up as a criterion by which to judge, in any given case, as to the fairness or otherwise of the remuneration that the labourer was getting. If we wish to realise how wide is this conception from the truth of the matter in the world as we find it, we have only to ask, why then is this criterion never by any chance referred to by any one in real life? If there is such a criterion available, why is not the question of the correspondence or otherwise of actual wages with it, the first question that occupies every one's attention whenever there is a dispute between capital and labour? Why did not Mr. Lloyd George two years ago, when he had to endeavour to settle a dispute in the cotton trade, begin by inquiring whether the men were getting as wages the equivalent of their marginal net product or not? For the simple reason, I think, that no one in the world could tell him what the

marginal net product was, or where it was to be found. No one certainly could lay his hand on any operative in the cotton trade, and say, 'This is a marginal labourer,' and much less would it be possible to say, 'This is his net product.' The theorists, in short, are found to be dealing, not with practical realities, but with empty sounds. The mistake they make is in treating as if they were matters of easy and familiar knowledge the contents of concepts which are absolutely and completely hidden both from themselves and from every one else.

Let us look at this conception of the marginal net product yet a little more closely. How is the conclusion that the marginal shepherd 'adds to the total produce a net value just equal to his own wages' arrived at? The method is this: we know, to begin with, what the shepherd's wages are. Say, for example, that they are 17s. per week. We then say to ourselves that the sheep farmer would not hire the man at that price and keep him on, from year to year perhaps, if he was steadily losing money by doing so. On this ground, we conclude that the value which the shepherd adds to the produce of the farm cannot be less than 17s. per week. This is the first step towards proving that it is just 17s. The next step is more complicated. We say to ourselves again something to this effect; that if the value that shepherds who can be hired at 17s. per week were adding to the produce of sheep farms, were more than enough to cover their wages with interest on the capital employed, the profits of sheep farming would be such as to attract additional capital into the business, and then wages of shepherds would go up to something above 17s. per week. As they have not done so, we conclude that what the shepherd adds to the produce of the farm is not more than 17s. per week, and as we have satisfied ourselves already that it could not be less, we conclude finally that it will be just that amount. Here, then, we have the net product defined and identified. We name the last hired man the 'marginal shepherd,' and proceed to lay down the general law that the wages of the marginal shepherd will always be equal to his net product.

Without going into the question of the flawlessness of this reasoning for the moment, let us concentrate attention on its nature. Absolutely the only fact before us is the fact that a shepherd has been hired in the open market at 17s. per week. From this alone, pure and simple, we have conjured up the whole story about the marginal shepherd and the net product of his labour. Of this elaborate conclusion it is clear that one of two things must be true, either that it is all nonsense from beginning to end, or else that, if translated into plain English, and understood with the due reservations, it is all in the context already.

We find the first reservation stated for us ingenuously enough by Professor Marshall himself. It is this, that the words 'net product' have, in this instance, 'no real meaning.'[1] They have no meaning, 'since, in order to estimate (a man's) net product, we have to take for granted all the expenses of production of the commodity on which he works other than his own wages.[2] In the example cited, our minds are fixed on the twenty sheep. We can think of them as a net product. But take some other example: take, say, the transport of cotton from New York to Liverpool, or the spinning of fine yarns yet finer; we have, then, no such resource. All that we can call the net product in such cases is the value of the services that the man renders, and this we confessedly know nothing about except as an inference from his wages. Professor Clark, who devotes hundreds of pages to the elaboration of the theory, adduces as furnishing a parallel to the marginal labourer and his net product, the case of the settler who takes up and makes a living off Homestead land when that is obtainable. There we have the theory of what is called in America 'Squatter sovereignty,' the theory that wages are kept up to a certain level by the fact that any one who cannot get employment at that level has the alternative open to him of taking up and cultivating land that he can get for nothing. That

[1] *Loc. cit.*, p. 518. He tells us that the theory is not a theory of prices, but if not, what is it? Professor Clark, on the contrary, thinks it 'sufficient to furnish a theoretical basis for a law of wages.' (*Distribution of Wealth*, p. 102).

[2] *Ibid.*, p. 518.

theory is itself open to attack on many grounds, especially on the ground that the rate of wages rules the sort of land, as regards both quality and position; that will be taken up quite as truly as the possibility of taking up such land rules the rate of wages. But at any rate we are here face to face with something tangible. The alleged determinant of wages is now a *vera causa* in as far as it goes. It is something that itself stands outside the sphere of wage-paid labour, and that, by absorbing part of the labour supply, no doubt, actually affects wages. But have we in the marginal net product with which it is proposed to co-ordinate it, anything that similarly stands outside the sphere of wage-paid labour. On the contrary, of course, we know that the marginal labourer is himself a receiver of wages, and, as to his net product, it appears to be, as regards its amount, nothing else whatever but his wages themselves. Yet we propose to set it up as a criterion by which to judge of their equitableness. If we had no better bulwark against the discontent of the masses than this fantastic story, 'society as it at present exists' would certainly be in a perilous plight.

The Marginal Shepherd not Marginal.—The next reservation is no less than this, that the marginal shepherd is not marginal at all. He is held to be not one whit inferior in efficiency to the shepherds that have been hired before him.[1] Finally, we learn to our amazement that the other shepherds were not hired before him after all. He is not the 'last hired man.' All the shepherds were hired at once. That, of course, corresponds to the state of things in modern industry much more nearly than the supposition of men being put on to work in factories one by one. Professor Clark remarks indeed that the device—his own device, of course, as well as that of the other theorists—of supposing labour to be put on unit by unit is 'purely imaginary.'[2] All the units are, in truth, precisely on a par, both as to efficiency, and as to the order of hiring. They are, in short,

[1] Professor Marshall says, 'The man is supposed to be representative,' to be 'a man of normal efficiency' (p. 516). Von Thünen lays down the same principle (*op. cit.*, 19).

[2] *Op. cit.*, p. 165. The remark is repeated on page 166.

absolutely indistinguishable the one from the other in every possible respect. The hypothesis of the final unit has been from beginning to end much ado about nothing.

It is strange that the theorists do not see that by this second part of their reasoning they have completely rubbed out all that they had sketched in by the first part of it. After these last-cited statements have been delivered, there cannot be, by their amended hypothesis, any longer either marginal labourers or final units of labour in existence, yet they continue freely and very extensively indeed to speak about both. All that remains of their theory now is the bare fact that when the supply of labour or of anything else is increasing, there must be some unknown and unknowable item which we may think of, if we please, as being the last added to the stock, though we have no reason to suppose that it is so really. The words 'final unit,' if they have any meaning left, mean merely the unit that by its arbitrary selection by our fancy as being the last addition to those that are already there, 'brings the supply up to its present magnitude.'[1] Prices and wages are, of course, other things being equal, determined by the magnitude of supply, and the whole story really means nothing else whatever but that this is so. It is nothing but a statement over again of the old and familiar law of the effect of supply on price.

Hypotheses in Economics.—The device of supposing labour to be put on unit by unit is indeed one of those intolerable 'hypotheses' adopted one moment, to be thrown overboard the next, with which the science is becoming infested. They are said to have some analogy to the inevitable hypotheses of natural science, to assist us in 'breaking up problems, and so to enable the study of the subject to be more effectively carried on. What they do really is to raise up out of nothing impenetrable fog-banks of verbosity, and to introduce and keep alive endless confusion of thought.

'An hypothesis in science,' John Stuart Mill observes,[2]

[1] Clark, *op cit.*, p. 180.

[2] *Logic*, People's edition, p. 149 *n.*

'usually means a supposition not proved to be true, but surmised to be so, because if true, it would account for certain known facts.' In the end, of course, such hypotheses are either proved to be true or dismissed as untrue. Science knows nothing of hypotheses confessedly untrue which, for all that, are not dismissed but, on the contrary, are descanted on as if they were true, through page after page, and chapter after chapter. There are, to be sure, it must be remarked, in science another class of hypotheses, a class which, as Mill thinks, might more properly be described as fictions. They comprise, for instance, the supposition of the existence in the real world of true circles, of absolutely straight lines, of a perfect vacuum, and so on. These, indeed, we continue to use, though we know that they are not literally exact. They are, however, so near the truth that nine-tenths even of the educated world believe them to be exactly true. They have, if possible, still less affinity than the first-mentioned class to hypotheses such as the one under consideration, the fancy that operatives in modern industry are always put on to jobs one after another, or that commodities are always bought in a series of infinitesimal increments. Such hypotheses as these are, of course, in flagrant contradiction to the notorious facts of life.

The Static State.—Another famous hypothesis that has been applied to the resolution of some of the difficulties that have arisen in connection with the marginal shepherd theory is that of the static or stationary state. It owes its origin, like the rest, to Von Thünen. If the assertion should be made that in real life the wages of the marginal labourer, and consequently the current rate of wages in any given grade of labour, must conform to the value of the net product of that labour, grave difficulties at once present themselves. An objector may say perhaps: 'I am not getting the same wages that I got last year, though I am turning out the same amount of work, and the price of the finished commodity has not changed.' 'Is it,' he may ask, 'to last year's wages or to this, that my net

product must be held to conform ? ' It certainly cannot be to both. Changes in wages, indeed, without any conceivable change in net product, occur whenever there is an influx of labour into a trade resulting in a fall of wages, or an absorption of labour by other trades resulting in a rise. The theorists, when confronted with such objections as this reply, ' We do not say that the theory corresponds accurately with the conditions of real life. It only tends to do so. It would, however, be seen to work with absolute accuracy in the static state.' The static state thus appears to be an excellent device for avoiding the necessity of bringing one's abstract statements to the test of comparison with actual conditions. What then is it ? One of its characteristics, we are told, is this, that in it ' labour and capital are absolutely mobile,' [1] that is to say, that in it a lawyer could take charge of a Dreadnought at a moment's notice, or a curate would, without hesitation, undertake to kill and skin a bullock. In the static state, too, the course of prices can be predicted for years ahead with perfect accuracy.[2] Professor Marshall tells us further that in the stationary state ' the demand lists of prices would always be the same, and so would the supply lists.' [3] But if that is so, how could there then ever be any variations in price at all ? In any case the supposition does nothing less than blot out at one sweep all economic phenomena. Von Thünen's theory does the same. In his static state, it seems, there would be no variations in the ratio of supply to demand.

After a human nature denuded of most of its usual characteristics has been brought on the scene, the question seems to have arisen in the minds of the theorists whether the conditions which rule at present in the solar system must not also be supposed non-existent. In one passage certainly changeless seasons are postulated.[4] What, however, is the object of all these suppositions. We are told that by making them we can best approach the study of economic phenomena ; but they leave us no economic

[1] Clark, *op. cit.*, p. 29.
[2] Marshall, *op. cit.*, p. 810.
[3] *Ibid.*, p. 367.
[4] *Ibid.*, p. 367.

phenomena to study. We might as well, indeed, begin the study of astronomy by supposing that there was no such thing as a law of gravitation, or begin the study of biology by supposing away heredity, variation, and the struggle for existence.

Before leaving the subject, it may be worth while to inquire by what special line of reasoning is it that Professor Clark satisfies himself that, though wages and the net product of labour do not coincide in the real world, they would in the static state. It is the following. He maintains that, in that state, the competition of entrepreneurs with each other would make profits fall away to nothing—why the entrepreneur should still continue in business in such circumstances he does not explain—and that wages would get what profits lost. But is this condition of things a static state? On the contrary, it is evidently a state of continuous change. By making population stationary, he eliminates any increase of the competition of labour with other labour, while by omitting to make a similar supposition about capital, he allows it to enter on, or to continue a course of ceaseless and remorseless competition with other capital. Evidently, however, if the one factor of production is made stationary, the other factor should be made stationary also; and, in that case, whenever capital in increased quantities was applied in one use, it would have to be withdrawn from some other use. Production, then, as regards the latter would be curtailed, prices would rise, and profits would re-emerge. It does not seem, therefore, that any of the things would happen in the static state which Professor Clark predicts. Economics, indeed, will stand very little in the way of hypothesis. As soon as we relinquish the guidance of the conditions of real life, we flounder, at once, in fathomless quicksands. In order, however, that it should be possible for us to keep continually in touch with the conditions of real life, it is essential that we should use nothing but the language of real life.

CHAPTER VI

THE MARGINAL UTILITY THEORY

What Marginal Utility is.—In our last chapter we considered the general doctrine of the margin as held by the economists of the modern school. In the present I propose to deal briefly with the theory of marginal utility. The transition from the margin to marginal utility ought, one would think, to be an obvious and easy one. As a matter of fact, it is far from being so. It takes a large amount of hard work to discover what marginal utility can have to do with a margin of any sort. One occasionally comes across writers on social or business questions such as Mr. Sidney Webb or Mr. Conant, the author of *Banks of Issue*, who have a fancy for bedecking themselves in the plumes of the economists, and they, we find, frankly use the phrase as the equivalent of the word 'value.' How it comes, however, to be a synonym for value is a mystery which they have not fathomed, and probably have no intention of fathoming.

To understand how the phrase has obtained its present meaning, one has to go into the history of the theory. What is now called marginal utility was, in the first instance, designated by Jevons, 'the final degree of utility,' and some economists, among them Mr. J. B. Clark, frequently use that designation still. The question that faces us then is this : what is the final degree of utility, and, whatever it is, how did it ever come to be used as a synonym for exchange value ; and, again, perhaps, if it is now used by the economists as such a synonym, is there any advantage in thus substituting it for the original expression ?

We have to conceive, to begin with, of the minds of the economists as being dominated by the project of ignoring the existence of money in their speculations. This fancy

the modern school inherited from the classical school. Business concepts, however, are there, and have to be dealt with somehow, and thus the problem faced these investigators from the first, how to deal with such concepts in non-pecuniary language. It did not apparently occur to them to inquire whether such concepts could have had any existence in a state of things in which money itself had not as yet come into existence.

In looking out for some non-pecuniary equivalent for exchange value, the thought of utility, of course, presented itself. Utility and value have, no doubt, a great deal in common; still, not less obviously, they are not identical. Many things are useful that have no value whatever, and many things have great value whose utility is as near as possible to zero. If value then could not be identified with utility straight away, and without more ado, might it not, nevertheless, they asked themselves, be identified with some phase or modification of it, and thus for a generation or more the economic world in England, in Austria, and in America has been engaged in a struggle to so manipulate the thought of utility as to extract from it the concept of monetary and measured values, without, at the same time, ever mentioning the word money. It is not the case, of course, that the thought of money is really left out of account altogether in the speculations of these writers, but rather that there is a curious surreptitiousness in the mode of its introduction. Like the unworthy teetotaller, with his glass of whisky, they use it while affecting to ignore it.

Exchange value then, as we have seen, in Jevons's view, was not utility generally; it was 'the final degree of utility.' What then, we must next ask, did he mean by this final degree? It is impossible to explain to any one what he did mean by it without, to begin with, citing his illustrative example or some parallel one. To the ordinary man using ordinary language, utility, of course, presents itself as possessing degrees innumerable between the highest and the lowest. The lowest or 'final' degree would, one would think, be found when the utility is at a vanishing point, and nowhere else. That, however, would not do for Jevons.

The vanishing point is certainly not his 'final degree.' To get at it, we have to suppose the case of two individuals, one of whom is being supplied with bread, let us say, the other with beer. The more bread you give to A, the less eager he becomes for any additional supply, while, at the same time, B is similarly affected by his increasing supplies of beer. At length a point is reached in the experience, say, of A, at which he will prefer exchanging for beer any more bread that is given to him to consuming it himself. Bread has then reached with him, its 'final degree of utility,' and if the desire for more beer has reached a similar degree in B's case, an exchange will take place. This, in the language of the theorists, is the 'law of diminishing utility.'

How it became a Synonym for Value.—We see, or seem to see, then this much, that the final degree of utility of anything corresponds to the point at which the owner prefers exchanging it away to retaining it, or to taking any more of it. It is viewed as a characteristic of the object exchanged, and corresponds to the sentiment in the subject exchanging, which is found in existence at the moment of exchange. It is this coincidence of the sentiment with the fact and the instant of exchange that alone renders its identification with exchange value plausible. Marginal utility, we see, thus only emerges when an exchange takes place, and it always emerges then. The expression, 'final degree of utility' was dropped because of its liability to confusion with the vanishing point of utility, and the phrase 'marginal utility' was substituted, the margin here being, in Professor Seligman's words, the point 'below which the consumer will prefer to abandon the use of increment for something else.' The theory gives no distinct account, it must be observed, of the marginal utility of the thing obtained in exchange. That appears to be looked on as a fixed point below and above which the other can range.

We thus find Professor Seligman laying it down that 'value' is the expression of marginal utility. Professor Clark speaks of the identification between it and value as

the 'law of value'; and Professor E. von Boehm Bawerk describes the same fact as the 'great law of marginal utility.' All of them endeavour to persuade themselves that they have solved the problem of getting at, and setting forth the philosophical basis of exchange value without ever once introducing the conception of money.

I have endeavoured so far to get into my reader's head some idea of what this marginal utility is conceived of as being, and on what grounds; and have not, up to the present, offered any criticism of the theory. The reader himself, however, will probably not have failed by this time to make, on his own account, one criticism at any rate. Marginal utility apparently, on the face of it, has no application to anything but homogeneous substances that are being ceaselessly and steadily absorbed from moment to moment by consumers. Where, however, are there such substances or such consumers? If, again, value and marginal utility are at bottom the same thing, value also can apply to homogeneous things only. A horse, a house, or a ready-made suit of clothes, could then neither be valuable nor valueless. Value could have no meaning at all as applicable to them. Leaving my reader to consider this point, I will proceed to offer some further criticisms on the theory.

The Reliance on Ambiguity.—We have seen that the marginal utility of anything is conceived of as being a character or attribute of it which springs into existence at the moment when it is about to be exchanged for something else, and that it thus corresponds to our estimate of the thing, or our degree of demand for it at that moment. Professor Seligman thus says, 'When we speak of demand, we think of marginal utility.' He does not explain why we should not, like other people, think of demand itself when we speak of it. At any rate, this much is clear, that marginal utility is something that springs out of and belongs to the individual psychology of the exchanger. If that is so, however, the question, of course, at once arises, how can we identify it with exchange value. If I have bread to

sell, I will soon find that its exchange value will not depend on any estimate of it, or demand for it on my own part, but on the action and reaction of the forces of supply and demand in the outside world. The manner in which the theorists meet this difficulty is interesting and characteristic. It has indeed become more or less unconsciously a sort of fine art with them to so construct every sentence that they use that these sentences should have a possible double application, one in the sphere of the individual psychology, the other in the sphere of the commerce and business of the world.[1] These double meanings are not to be regarded as anything in the nature of casual and accidental errors. They are the very breath of life of the theory itself.

When the theorist is engaged in setting forth his principle as the Great Law of Value, or as its psychological basis, then he conceives of and explains marginal utility as something that corresponds to his own demand for, or estimate of, the thing parted with in exchange. With regard to this estimate, he can, of course, be conceived of as possessing some sort of *a priori* knowledge. When, on the contrary, he is driven to explain how his theory can be made to fit the facts of life, he then begins to talk about 'social' demand, and he soon lets it appear that what he now conceives of as marginal utility corresponds, not to his own demand at all, but to *the demand of other people*. Now it is quite certain that he cannot have things both ways. In assigning a meaning to marginal utility, he must take his choice between his own demand and other people's demand. If the marginal utility of bread, for example, means my own demand for bread, then it certainly can have no affinity with exchange value. Nothing is more certain than this, that it is not my own individual demand which determines, or indeed in any practical manner affects, the price of bread

[1] I am not alone in this view. Professor Veblen, as we have seen, refers to ambiguity as the basis of Fisher's doctrine of interest. Dr. Davenport, too, in his comments on Boehm Bawerk and Wieser, has to make the complaint on almost every page that their point of view in this respect 'seems to be in perpetual flux.' See *Value and Distribution*, pp. 340-370.

in the world at any given moment. If, on the contrary, it is the demand of other people generally that is to be held to be that which corresponds to the marginal utility of bread, then, how can that fact be put forward as the explanation of the psychological nature of value? Other people's demand is something that you and I know nothing whatever about before the event, before the sale or the purchase, that is to say, in which it plays a part. To put this sort of demand forward as the explanation of the inner character of value is to put forward mere empty sound, words whose meaning corresponds to nothing real.

As illustrative of the dependence of the theorists on their double meanings, we may cite the following from the most competent of them all, Professor Marshall. 'With every increase,' he remarks, 'in the amount of a commodity its marginal utility falls,' and 'with every fall in that desireableness,[1] there is a fall in the price that can be got for the whole of the commodity.'[2] Both the tenor and the order of this sentence certainly import that what happens is this; that a change in supply changes my own feeling with regard to the importance to me of a given commodity, and that that change in my own feeling causes a change in its price. But this, of course, is quite obviously untrue, and, indeed, altogether unlike the truth. When this objection is urged, however, the defence is at once put forward that what is meant is not that the increase of supply changes my own sentiment with regard to the thing, but that it changes the sentiment entertained towards it in the outward world, and so changes its price. Marginal utility, let it be conceded, may stand as the equivalent of demand. We must, however, have an unambiguous answer to the question, Whose demand? Is it our own demand, or the demand of the outside world that is in question? To treat it as our own in one breath, and as other people's in the next, is a proceeding that cannot be looked on as legitimate.

[1] Note the identification of marginal utility with 'desireableness.'

[2] *Loc. cit.*, p. 141.

Wieser on Marginal Utility.—We have arrived, then, at the conclusion that the leading idea of the marginalists throughout is that of presenting monetary phenomena in a non-monetary guise. It will be of interest therefore to take a phenomenon that most of us would say, at first sight at any rate, was beyond all question a purely monetary one, and to observe how the theorists—this time Austrian theorists—deal with it, how they seize upon it by the strong hand, as it were, and, right or wrong, force it into their non-monetary mould.

The phenomenon is the familiar one presented when a glut knocks down the value of the total crop to a figure perhaps very much below that at which the half, or even the quarter, of it might have been placed if the balance had failed to mature. In such cases we know that it has often enough happened that the growers have combined to destroy a great part of their crop with the express purpose of raising what remains to a higher figure than the total could have reached otherwise.

Viewed as a monetary phenomenon, the case, of course, presents no difficulty. The commercial value of the crop is represented by the total quantity of money that it will fetch. There is no mystery in the fact that a greater total quantity in the hands of various sellers may fetch less than a smaller quantity would. The sellers may come tumbling over one another to get something for their redundant supplies, while yet anything is to be got, and, rather than find them left on their hands unsold, may let them go for next to nothing.

When we address ourselves to the self-imposed task, however, of explaining the manner in which a parallel state of things could come about, when we do not take the existence and operation of money into account, we find that our problem is by no means a simple one. Let us see how Wieser sets about it.

In introducing his reasoning I may, in the first instance, recall to my reader's remembrance our attempted elucidation, in a former chapter, of the manner in which the marginalists set forth the ancient and famous law of supply

and demand ; how they express the simple fact that value ordinarily declines as supply increases. As regards the application of their theory to wages, we found that the case was put in this way. It was held that if the labour supply were, at any time, increasing, there must necessarily be some unknown and unknowable units that were being added to those already there. That, of course, is all contained in the signification of the verb 'to increase.' Further, we know from general experience, that wages or prices usually fall, other things being equal, with the increase of the supply. The theorists, therefore, hold that they may say, if they please, that the units last added, in our fancy—the marginal units—are of lower earning power than those already there ; but that when they are added to the rest, their status is taken by the whole number.

We cannot for a moment admit that this is a legitimate method of putting the case. There is no reasonable ground for substituting a series of fanciful steps for the smooth flow of increasing supply, nor is there any accordance with truth of any sort in the conception either that the one unit selected arbitrarily as that which we will designate 'the last added,' has a lower status than the others, or that its addition miraculously communicates this lower status to the rest.[1] These, however, are Wieser's assumptions. Presenting the case of the increasing stock of a commodity, and the consequently descending scale of its degrees of utility, he calls the utility of the first portion possessed the first degree of utility ; that of the next added, the second ; of the next again, the third ; and so on. He then goes on to assert that whenever an increment is added, the marginal utility of the whole stock is at once brought down to that of the lowest part. He illustrates this by a scheme of figures, the gist of which is this : [2] A man may be supposed as owning one good, say, one loaf of bread, the utility of which may be set down at 10. We may next suppose that

[1] This miraculous transmission of value, as if it were a fluid, is a conception of the Austrian school and the quantitative theorists generally, to which we will have to revert later on.

[2] *Natural Value*, Eng. trans., p. 28.

his holding gradually increases up to 11 goods, in the course of which increase the addition of each good is attended with a diminution of one degree in the marginal utility of the whole stock. The result will work out as follows :— When the individual has the one good only, its value, as we know, is 10. When he has 2, the value of the 2 will not be 20, but 18. If we go on adding goods up to 6, the value of the 6 will be 30. Add now, however, another 5, so that the man has 11 goods—11 loaves, say. What will the value of his whole stock be then ? It will, we are told, be nothing at all ! This surely is a conclusion fitted to stagger humanity. We may well ask, does it correspond to anything either in actual or in conceivable experience ?

The answer will be made : that it corresponds to the phenomenon that we have been dealing with, the effect of a glut in cutting down the value of a whole crop to a lower figure than that which would have represented the value of a part of it. But what resemblance is there in reality between the two cases ? Obviously two things that are as wide as the poles asunder are confused with each other. The fact of simple possession is confused with the operation of the forces of supply. In the case of a bumper harvest, say, with a narrow market, the value of any one farmer's crop of wheat may, of course, be brought down even to zero by the competition of other sellers, all of whom are in possession of more wheat than they know what to do with. The competition of sellers thus acts as an extraneous force on value in each individual case, pressing it down to lower and ever lower levels. But what is there that corresponds to this extraneous force in the case under consideration ? The supposition is that a man, an hour ago, had 6 loaves of bread, and that their value stood at 30. Now he has 11, and their value stands at nothing at all. The last added 5 loaves not being wanted, are valueless. That may be admitted ; but by what conceivable process are they supposed to transmit their valuelessness to the 6 that were there before, some, at any rate, of which are, by hypothesis, indispensable for the preservation of the man's

life. Professor Seligman follows Wieser in this exhibition of dialectics. He tells us that the marginal utility to a man of 8 apples may be actually less than that of 5 of their number.[1] He might just as well tell us that the whole may be less than the part.

Marshall's Enigmatical Attitude.—A survey of Wieser's reasoning, such as that set forth above, is important, if only as giving us a clue to Professor Marshall's treatment of the subject. Marshall does not follow Jevons, Boehm Bawerk, or Wieser in giving us any elaborate exposition of his own, with illustrative examples, of the nature of marginal utility. He takes that ready-made from the Austrians, so that his line of thought on the subject is not comprehensible without reference to the expositions of these writers. Among the few explicit statements to which he commits himself, the most significant is this, that 'that part of a thing which (any one) is only just induced to purchase, may be called his *marginal purchase* . . . and the utility of his marginal purchase may be called the *marginal utility* of the thing to him.'[2]

Surely, however, my reader will say, two things are here identified, the identity of which is not, to say the least, on the face of it, obvious. The first is the utility to a man who has already, say, four loaves of bread, of a fifth loaf; while the second is the marginal utility to him—whatever 'marginal' may mean—of bread in general. The first is a characteristic predicable of a particular loaf in special circumstances, the second is an attribute of bread conceived of as a universal. What connection can there be between the two? By what sort of feat of mental gymnastics can one pass from a conclusion in regard to the one to a conclusion in regard to the other? Wieser's reasoning makes the feat perhaps comprehensible, if it does not justify it. Marshall's conclusion, indeed, is an echo of Wieser's doctrine that the fall in value attendant on an increase of supply may be viewed as the transmission to all the items in any stock of the relatively low status of the item last added.

[1] *Loc. cit.*, p. 181. [2] *Loc. cit.*, p. 93.

The item last added is, in other words, the 'marginal purchase,' and its degree of utility becomes, in Marshall's language, the 'marginal utility' of the whole.

Let us see, however, to what sort of conclusions this description of logic is calculated to conduct us if we follow it out to the bitter end. Let us suppose an exchange to take place of an increment of sugar for an increment of salt. These increments are both 'marginal purchases,' and the simple fact of the exchange seems to warrant us in asserting that the utility of the one is just equal to the utility of the other.[1] But if, in each case, the marginal utility of the 'thing,' that is, of the universal, is defined by the utility of the marginal purchase, then the marginal utility of sugar would be just equal to the marginal utility of salt; and, by parity of reasoning, the marginal utility of gold must be just equal to the marginal utility of silver or of iron. In fact, the marginal utilities of all exchangeable commodities must be equal *inter se*. If, again, we are to hold, with the theorists, that marginal utility is coincident with exchange value, then it follows that the exchange values of all commodities must also be equal to each other! Here, however, beyond question, we are face to face with a *reductio ad absurdum* of the whole marginal utility theory, if only the *reductio ad absurdum* itself had a definite and recognised place in the discussions of economics.[2]

An Antinomy.—In the statement of the above argument, we have taken it for granted that if two increments of two different commodities are exchanged for one another, the fact of the exchange itself is proof sufficient that the respective utilities of the two increments are equal to each other. All the things bought, for example, at the same time by one purchaser for a shilling each are always looked upon by the theorists as having the same degree of utility, because the utility of each is equal to that of the shilling. This,

[1] See Jevons, *Theory of Political Economy*, p. 138.

[2] Professor Seligman shows himself to some extent alive to this difficulty, but does not succeed in getting rid of it.

of course, is Jevons's view,[1] and is that generally set forth and universally assumed. We have now entered a region, however, where contradictions and inconsistencies are the rule rather than the exception, so that it need not surprise us to find that, in other expositions of the theory, a proposition that directly traverses this one is put forward as, at any rate, equally self-evident with it.

We are told that no exchange ever can take place unless the marginal utility of the two things exchanged is different; unless, that is to say, that of the thing obtained in exchange is greater than that of the thing given for it. Boehm Bawerk, for instance, tells us that 'an exchange is economically possible only between persons who put a different value, even an opposite value upon the commodity and upon the price equivalent.'[2] There is, of course, much force in this reasoning. Why should a man go out of his way to exchange a thing for money, if the money, when he has got it, is of no greater utility to him than the thing itself would have been. It is obviously because in such a case the utility of the money is greater than that of the commodity bought that he exerts himself to effect the exchange. But then the trouble is that this introduces for us an absolute divorce between marginal utility and exchange value. How can we go on describing the second as simply an expression of the first, if they are necessarily to some extent divergent, and maybe as far as the poles asunder. What is called the 'consumer's rent' is that which marks the degree of the divergency. The reader can place for himself the two theorems, with their respective lines of reasoning, in parallel columns, like Kant's antinomies, or like the extracts from his speeches, with which the ingenuous parliamentary candidate usually finds himself confronted.

Here, to our infinite surprise, Professor Marshall comes on the scene in a new character. He has been using the

[1] He states it thus: 'The possessors of any divisible commodity will exchange such a portion of it that the next increment would have exactly equal utility with the increment of other produce which he would receive for it' (*Theory of Political Economy*, 2nd ed., p. 149).

[2] *Positive Theory of Capital*, Eng. trans., p. 195.

language of the theory. His own doctrine of wages, of price, and of value is, to all appearances, based on it. Now, however, it seems, he will have none of it. 'We cannot speak of price,' he says, 'as measuring marginal utility in general, because the wants and circumstances of different people are different.'[1] Would it be possible to recognise more explicitly the divorce between the two, or to give a more flat denial to the assertion that the one is simply the expression of the other? Professor Marshall would answer, 'I never made the assertion quoted, nor any other precisely like it.' Literally, perhaps, that is true, but what are we to make of his assumption that the 'law of diminishing utility,' as he calls it, can be without more ado, 'translated into terms of price?' Does this not imply that the marginal utility theory can be used to explain the inner nature of value in exchange. In his *Note on Ricardo's Theory of Value*, towards the close of his work, we find him adopting an attitude towards the theory that is very like one of downright hostility. 'Jevons,' as he says, 'supposed himself to be getting nearer the foundations of exchange value when, in his account of the causes that determine it, he substituted the phrase "final degree of utility," for the price which consumers are only just willing to pay, the phrase which in the present treatise is condensed into "marginal demand price."'[2] Again, he remarks that perhaps the same writer's 'antagonism to Ricardo and Mill would have been less if he had not himself fallen into the habit of speaking of relations which really exist only between demand price and value, as though they held between utility and value.'[3]

If language has any meaning, surely this means nothing else but that the idea that runs through the writings of Jevons and the Austrian school, that they have discovered something that stands behind exchange value and explains it—that is, in short, its psychological basis—must be discarded; and, further, that the value of a thing must be held to be simply what it will fetch and nothing else. That, indeed, is what alone coincides with the writer's formal

[1] *Loc cit.*, p. 100. [2] *Ibid.*, p. 818. [3] *Ibid.*, p. 820.

definition of demand price.[1] This doctrine is one that will, no doubt, commend itself to the business world, but it is surely a strange one to find emanating from its present quarter. If it is valid, why not drop, at once and for good, all the phraseology based on the marginal utility theory? If it is valid, again, what becomes of Professor Marshall's own application of the theory to the problems of distribution, an application so important, in Professor Clark's view, that 'the right of society to exist in its present form' may be said to depend on its capability of being sustained.[2] If we are to substitute demand price, that is to say, the price which in any given circumstances it is possible to obtain, for marginal utility, as the basis of value, we may, I suppose, also substitute it for marginal productivity, which is the same thing as marginal utility with a special reference to labour. We should then apparently have Professor Marshall's authority for holding that a man's wages are determined and justified in the long-run, not by the marginal productivity of his labour, but simply by the fact that they are just what he can get.

The danger of deserting natural language is brought home to us forcibly by inconsistencies and contradictions such as those dwelt on. They crop up continually in connection with the use by the theorists of their artificial terminology. One inconsistency encounters us at the very outset of the discussion. If marginal utility and exchange value are so related that the second may be called the expression of the first, then, surely, it follows that price is always marginal. If so, however, what is marginal price? Is it marginal 'marginal utility'? When an exchange takes place, it does so because the desire for an additional portion of some one commodity has reached a 'limit or margin as compared with the desire for some other commodities.'[3] Marginality must surely, therefore, be universal in the case of exchange. Nevertheless, we are con-

[1] *Loc. cit.*, p. 95.

[2] *Distribution of Wealth*, p. 3. Professor Clark, of course, refers to his own exposition of the theory, which at this point, however, coincides with Professor Marshall's.

[3] Seligman, *Principles of Economics*, p. 178.

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tinually finding the word ' marginal ' applied to prices even by the most careful writers of the school, as a differential adjective, used, that is to say, to distinguish the so-called marginal prices from those that are not marginal. Professor Marshall, for example, in one passage, tells us that ' in every case the cost of production is marginal.' [1] Yet we find him a few pages farther back using the expression ' marginal costs,' implying, of course, that there are costs which are not marginal ; and if he finds the consistent use of the phraseology impossible, we may be sure that the other writers of the school possess no advantage over him in that respect.

Another inconsistency arises in connection with the same distinguished writer's application of the expression ' marginal utility ' as regards capital. The marginal utility of money is, of course, universally said to be least to those who have most of it. Professor Marshall, however, has occasion to remark that a rise in the rate of interest ' will cause capital to withdraw itself partially from those uses in which its marginal utility is lowest,' [2] that is to say, those uses in which it is earning least. Here, plainly, the phrase takes on a fresh signification altogether. It is obviously not our richest men who are making least out of their capital, as it should be if this use of the expression were legitimate. Beyond question, M. Bréal is right in maintaining that the ' people's distinctions are the only true and the only good ones.' The theorists' distinctions never retain precisely the same meaning on any two consecutive pages.

Is Marginal Utility Proprium or Accidens ?—If my reader is not thoroughly sick of marginal utility by this time, perhaps he will be ready to follow me in this last investigation into its nature, and then we may hope to be able to dismiss it for good. It has one outstanding peculiarity in the fact that it has no adjective corresponding to it. No theorist ever speaks of anything as being ' marginally useful,' nor would even any other theorist understand him if he did. In this respect the expression differs, of course,

[1] *Loc cit.*, p. 373. [2] *Ibid.*, p. 534.

from goodness, beauty, ugliness, and everything else of the sort. The truth is, it is a chimera born of the illegitimate blending of universals and particulars. Both Jevons and the Austrian economists started off on their line of speculation with some such intimation as this, that they intend to use the word 'utility' not in its ordinary sense, but as stripped of all 'its ethical and prudential connotations.'[1] In the new sense of the word, the 'utility' to any one of bad whisky would have to be held to be quite as great as that of wholesome bread, provided only that he wanted it as much. They did not realise, I think, how far, as viewed from the logical standpoint alone, this diversion of meaning would take them.

How did it happen, one may ask, that it should ever have been found necessary or desirable to divert a word from its ordinary signification in order to make it express the characteristic that is expressed under the theory by the new 'utility,' that is to say, the characteristic of want-satisfying power or agency simply, apart from the consideration whether or not it was beneficial or injurious to the object of it? Is there no word in common use that expresses this already? There is none, certainly, that expresses it directly. Have not, then, the economists in the past ever had any occasion to speak of such a thing? They have assuredly, and one of the very commonest of economic terms has always been in continual use in discussions with reference to it. It is the term 'demand.' An inversion of the sentence, however, is necessary in order to make use of it in the place of 'utility.' By such an inversion it can always be made to express the thought which Jevons and the Austrian school endeavour to express by that word. When they would say that the 'utility' of A to a man was greater than the 'utility' of B, other economists would have said that the man's demand for A was greater than his demand for B. The more natural method of expression,

[1] The words are Professor Marshall's (*loc cit.*, p. 92). They appear in a sidenote, and have, curiously enough, nothing in the text to correspond to them. Professor Marshall, from the first, accepted the diversion of meaning with reluctance.

moreover, we may always be sure, will in the end prove the preferable one.

Sir Leslie Stephen on the Theory.—I happen to have before me, at the present moment, a copy of the English translation of Professor von Boehm Bawerk's *Positive Theory of Capital*, which was at one time the property of Sir Leslie Stephen, and which has been presented by his family to the London Library. There is a written intimation on the title-page that the sidenotes in pencil in the book are his, and so, I presume, they may be regarded as public property. There is one, at the end of the third chapter of Book III., the chapter on the 'Amount of Value,' which is of some interest in connection with our present subject. It runs as follows :—

'Qy.—The difficulty in all this comes, perhaps, from the primary ambiguity of considering value as a property of the object instead of the subject. There is no difficulty as regards desires or about the things, but there is when the two points of view are blended.'

The expression is elliptical, but the general idea is a true one. The difficulty of the Austrian theory is due to the fact of its involving a continual attempt to express the variations of demand for a commodity on the part of the subject in terms of the 'utility' of the commodity regarded as a property of the object.

Let us try to follow this out a little more closely. Aristotle draws a distinction between the 'property' and the 'accident' which, in its main features, is still valid for Logic.[1]

An example of the attribution of the 'accident' is to be found in the affirmation that 'Socrates is sitting,' or that 'Socrates is laughing.' An example of the attribution of a property would be the statement that Socrates has the power of sitting or the power of laughter (risibility). An accident is, thus, an event, a transitory state, an affair of the passing moment, while a property is durable. In

[1] *Topics*, book I. chap. v. Lotze remarks that 'Translators torment themselves in vain to find an equivalent for both the real and etymological sense of Aristotle's expression *συμβεβηκός*. What is important and true in it answers completely to what we call *state*' (*Logic*, Eng. trans., vol. i. p. 54).

ordinary circumstances we express the accident by means of a verbal form, the property by an adjective. If the property should not be literally durable, like the colour of the sky, or of the fields, we think of it nevertheless as durable by thinking of it as a power possessed by an individual, and exercisable at any moment, the power, as in our example, possessed by Socrates of sitting, or his power of laughing.

Now, it is obvious that the predication of utility, either of the marginal, or of any other variety, in regard to any object is, correctly speaking, the predication of a property. When we affirm the utility of bread or of water, we affirm nothing but the power inherent in these substances to satisfy hunger or thirst. We cannot, by such a form, express the affirmation that they are at any given moment satisfying these appetites, much less that they are satisfying them in some particular case, and in some particular degree. In affirming risibility of Socrates, we do not affirm that he is laughing at this moment. That is reserved for the verbal form. What is it, however, that the theorists attempt to express when they attribute to anything 'marginal utility'? It is evidently not a property, but an accident, not a power, but a passing state. This is the real meaning of Professor von Boehm Bawerk's curious description of it as a 'casuistic'[1] affirmation, one, that is, that varies ceaselessly from case to case, and from moment to moment. The true property never does anything of the kind. The utility of bread is something that in natural thinking is conceived of as permanent and invariable, its marginal utility, in the theory, on the contrary, is something that is intense one moment, when supply has run short, non-existent, perhaps, the next, when supply is redundant. It is the analogue, not of the 'risibility' of Socrates, of his power of laughter, but of the fact that he is laughing at a given moment. The whole mystery of the theory, as Sir Leslie Stephen divined, is to be found in the fact that the theorists endeavour to use adjectival forms, predicating properties of an object in cases where every one else would

[1] *Positive Theory of Capital*, Eng. trans., pp. 139-140.

use verbal forms predicating variations of sentiment, or desire on the part of the subject. If, therefore, the tyro in economics finds himself bewildered by the strange language of the theorists, he may console himself with the reflection that no one really can see through it any further than he does, for the simple reason that it runs counter to the fundamental principle by which the reaction of thought on the matter presented to it results in the articulation of the latter into things, properties, and events.[1] For the theorists this deep-seated distinction between the property and the event, state, or accident, apparently does not exist. The two are for them hopelessly and gratuitously commingled. Of course, if a writer insists on treating the fact, say, that the quarter of wheat has risen during the past six months by ten shillings, as one of the permanent properties of wheat, he need not be surprised if he finds that he has become incomprehensible to all except those who share the eccentricities of his mental development.

[1] Lotze, *Logic*, Eng. trans., p. 17. The whole chapter will well repay study in this connection.

CHAPTER VII

THE MECHANICAL CONCEPTION OF VALUE

Wieser and Boehm Bawerk. Strange Dialectics.—In connection with Professor Wieser's exposition of the Law of Diminishing Utility, as the theorists call it, we had occasion to notice his curious assumption of the possibility of the transmission of high or low value from one object to another without any intervention of competition, or any conceivable opportunity for the operation of the forces of supply and demand. A man, we are told, was supposed to have 6 loaves of bread, and their marginal utility, or value, was said to stand at 30 ; you give him 5 more, and then the whole stock of 11 loaves becomes at once worth nothing at all. The valuelessness of the redundant loaves was, in such a case, conceived of as having miraculously transmitted itself to the rest.

The same conception of miraculous transmission manifests itself throughout a vast area of economic reasoning, but often in a very much more subtle form than the above. Suppose a duty of 2d. per lb. is put on to tea, next day the grocers raise the price by 2d., and we all, perhaps, think of the tax as finding its way directly into the price, in a fashion that, when we reflect on it, partakes of the supernatural. This comes from the universality with which we discount the future. In reality the connection between the tax and the rise in price is not thus immediate. It rests ultimately on the operation of the law of Supply and Demand. Suppose the case of an inexperienced world ; the middleman there, we would find, would probably be caught by the duty in the first instance. The next time, however, that he went into the market, he would offer less for the commodity. Production would thus be checked somewhere,

and supply would be curtailed. The least advantageously situated producers would, in such circumstances, cease producing. In our day age-long experience has told us a thousand times over that all this will happen, and so the rise in price takes place at once. We have not to wait for it till supply has sustained an actual check. All the same, the connection between the imposition of the tax and the rise in the price of the product consists of a chain of causation of several links. It is mere illusion to speak of the tax as literally 'entering into' the price. When we hear it asserted, therefore, that 'rent' does not 'enter into' cost of production, but merely affects it indirectly,[1] we are impelled to reply that no charge of any sort ever does, or can, enter into the cost or price of anything in any other sense than that of indirectly affecting it.

Value an Electric Fluid.—The conception, then, of costs as entering into price, we may set aside as unsound. What next of the doctrine that price enters into costs. In the exposition of that view neo-scholasticism, as it seems to me, has attained 'the limit,' if one may avail himself of an expression that has of late become something less than classical. Professor von Boehm Bawerk, in one passage, expresses himself to the effect that the value of the ultimate product 'is *conducted* to all the groups of means of production'; [2] that is to say, that the value of steel rails, for example, is conducted back into the value of the iron ore, the coal and the labour used in their production. Mr. Hobson remarks on this 'as an almost materialistic conception of value,' and no wonder. One cannot escape the conclusion that what is running in the eminent professor's head is the conception of something uncommonly like an electric fluid.

Of course it must at once be said that the conception of value as being conducted back from the ultimate product into the factors of production roughly corresponds to an important truth. Every one knows that a marked rise in the price of steel rails may easily cause increased activity in the iron trade, and may thus bring about not improbably

[1] Marshall, *loc cit.*, 437 *n.* [2] *Capital and Interest*, Eng. trans., p. 185.

a rise in iron ore, and perhaps also in labour. This way of stating the case, however, is not nearly good enough for the Austrian theorists. To understand aright the nature of their contention, we have to look at the use that they make of their reasoning.

An extraordinary amount of difficulties, to begin with, are raised in regard to the admission of the simple truth that capital is productive. That it is productive or capable of being productive is, of course, a truth embodied in the very meaning of the word. If it were not capable of being productive, it would not be capital. That it is, or can be, productive thus, is not a theory of J. B. Say's, or any one else's, but is inherent in the meaning of a common economic term as employed in every European language. On what ground, then, can the proposition be disputed? The reasoning runs something to this effect.

Say that the value of steel rails is £6 per ton, and let us suppose that of this £6, £4 is conducted back into labour, rent and interest, and the other £2 into the value of the iron ore and coal that are used. The whole £6 per ton, at any rate, the price of the rails, will be thus by hypothesis absorbed; it will be conducted back into the factors of production. Of course if this were the universal rule there would be no such thing as profit in any branch of industry. The value of the capital goods sunk in any undertaking, with interest on borrowed money, would always be fully equal to any possible price that could be obtained for the ultimate product.

To convince my reader that I am not in any way misrepresenting Professor von Boehm Bawerk's reasoning, let me quote some of his own words. To myself, on first perusal, they sounded altogether incomprehensible. Possibly to my reader, with the assistance of the above example, they may be less so.

The higher, he says, the apparent productive power of capital 'raises the value of the product, the higher must it raise the value of the capital itself as identical with it,' and therefore 'however great the productive power of capital may be, and however greatly it may increase the minuend

(the price of the ultimate product), yet so far as it does so, the subtrahend (the cost) is increased in the same proportion, and there is no remainder, no surplus value.'[1] That is to say, that whatever price you get for your product, this price is bound to have had the truly magical effect of raising your costs to an equal amount with itself.

But, we cannot help asking, where does the use or the sense of telling us this preposterous story come in? We know that nothing like it normally, or even frequently happens. If it did happen universally, production, of course, would stop dead, and never start again. The theorist has thus at the best, merely elaborated a *reductio ad absurdum* of his own theory.

Causation working backwards in Time.—When you examine the theory at closer quarters, you find that the writer not only makes the assumption that the value of the ultimate product will be conducted back intact, and without any possible deduction, to 'the groups of means of production,' but also that the value of the rails, for example, will be conducted back into the value of the very labour that made them, labour that, of course, has ceased to exist. He presents us, in fact, with a case of causation—if it is causation—literally working backwards in time, and raising the price of things now non-existent.

Viewing the series of facts as any one else would view them, as presenting a case of ordinary cause and effect, none of the problems or difficulties raised even remotely appear to emerge. No one would ever dream of arguing that, because the price of steel rails had risen from £4 to £6 per ton, the extra £2 would automatically add itself to the iron ore, the coal and the labour of the past in such a manner that there would be no profit left in the transaction. The truth is, of course, that it is not the iron ore, the coal, or the labour used in producing these particular rails that it would affect at all, but other iron ore, other coal, and other labour altogether. To-day's price of rails might, no doubt, affect next week's prices for ore, coal, and labour. But would

[1] *Loc. cit.*, p. 180.

any one dream of imagining that it would necessarily raise their price to such a height as to leave no profit, no 'surplus of value,' in rail production. This backward 'entering' of price into costs is a travesty of Marshall's forward 'entering' of costs into price, and is, no doubt, a good deal more absurd.

The account of such a specimen as this of marginalist dialectics would be amusing if it were not inevitably accompanied by the reflection that the time of so many candidates for honours at so many of our universities, which, with advantage both to the nation and to themselves, might be occupied by them in gaining a practical acquaintance with finance, or in mastering the mechanism of credit, is wasted out and out in hopeless attempts to solve these inept conundrums.

Cairnes, Newmarch, Addington, Marshall.—Referring to the effect of demand and supply on prices, Cairnes remarks, in a note to his *Essays on Political Economy*,[1] 'According to Mr. Newmarch, the depreciation of money may occur by a process which is neither of these, when money operates upon prices neither through demand, nor yet through supply, but "by reason of augmented quantity."' 'I must confess myself,' he adds, 'wholly unable to conceive the process here indicated.'[2] Cairnes, it will be seen, assumes the necessary intelligibility of causation in economics. He takes it for granted that if an alleged process of causation is one that a man of ordinary capacity cannot follow out in thought, it may be dismissed as mythical. The quantitative and mathematical theorists admit, of course, no such doctrine. Their whole line of reasoning is based indeed on its negation. The theory of the Appreciation of Gold, which was so much in evidence in the eighties of last century, rested on the alleged fact—alleged, no doubt, largely in error—of the accompaniment of the falling off in the gold production by a simultaneous fall in the prices

[1] Page. 57.

[2] It is strange to find Tooke's collaborator arraigned on this charge, and apparently with justice.

of commodities.[1] The sound money party urged that, even admitting such a conjunction, it was not in itself sufficient to establish the causal connection between the two. One must see, they held, *how* it was that the fall in gold production got at the prices of commodities to alter them; or, as Lord Addington put it,[2] 'you must show the *modus operandi*. You must set forth the process of reasoning, the motive which impels a seller to accept, except upon the issue of a struggle between supply and demand, a lower price for his goods in the face of an abundance of capital and a low rate of interest.' Professor Marshall, it will be remembered, felt the force of this reasoning to such a degree that he made the admission that the only way in which variations in the gold supply could affect prices was through the rate of discount. The trouble, however, is that, in this case, as M. Yves Guyot points out,[3] the cheap money instead of causing high prices, will ultimately cause cheap production and low prices, while dear money will tend to reverse these results.

Mill on the Actual Supply.—Mill's doctrine that, while the value of all other things is determined by the potential supply as well as by the actual, the value of money is determined by the 'actual' alone,[4] is another theorem that rests on the conception of the possible unintelligibleness of economic causation. The postulated operation of the actual supply cannot be conceived in psychological terms, for the simple reason that no one can know what the actual supply is till the transaction is over and done with. Wheat, for example, which enters the wheat market, but which is not sold must, of course, be looked upon as part of the potential supply only. We can understand without difficulty how the amount of the potential supply can act on the minds of sellers, and can, in the case, say, of its redund-

[1] Between 1890 and 1898 the gold production more than doubled while the Economists' index numbers (reduced to percentages) fell from 101·6 to 85·9.

[2] In a memorandum submitted to the Gold and Silver Commission of 1888.

[3] *La Science Economique*, 3rd ed., p. 198.

[4] *Principles of Political Economy*, book III. chap. ix. sec. 3.

ancy, make them fix their prices at lower figures than they would otherwise; but how the actual supply, which is only recognisable when looked back upon after the event, can affect them, it is impossible for any one to conceive. All the prospective supply is potential, and to assert that any supply that is not prospective can have any bearing upon the calculations either of sellers or buyers, is to assert with Boehm Bawerk, that causation can work backwards in time.

The theorist accordingly, in such a case, does not attempt to follow out the mental process that accompanies the determination of price. He falls back upon metaphor. He says, perhaps, that the influx of money into a country may be likened to the influx of water into a cylinder. As the inflowing current raises the water level, so the inflowing money raises the price level. How, psychologically, this happens, is left unexplained. We shall, however, have to deal in more detail with the quantity theory of money in a later chapter to be introduced in connection with the effect of credit on prices. In the meantime, we may remark on the fact that the acceptance as valid of causation that is psychologically inexplicable, but which owes such plausibility as it possesses to physical metaphors, is an unfailing mark of the quantitative theorists of every shade. The mathematical school are one species of that genus, and its older members, we know, were all bimetallists [1] so long as it was possible for any one to be so.

Supply conceived as acting directly on Value.—The supposed operation of money on prices, not through competition and the ordinary action of supply on demand, but simply 'by reason of augmented quantity,' is only one illustration of a vastly widespread, though palpably fallacious conception, the conception, namely, of supply as acting directly on value instead of operating as it does always and only through its action on demand. The current view of demand and supply as two co-ordinate forces that bear similarly on value, though in opposite directions like 'the blades of the scissors,' is one that will not bear examination.

[1] Or symmetallists.

Demand plainly lies closer to value than supply does. It is indeed nothing else but value as yet ungraduated. Increase the demand for anything in the world, and its value necessarily reaches a high figure; increase the supply, and most probably its value will fall, but, at the same time, it may not. Nothing in that case is certain. As M. de Launay points out, during the last ten years the annual supply of most of the industrial metals has doubled itself or thereabouts, while their value per ton has, in some cases, about doubled itself also. Give more bread to a community, and you will modify the demand for it, and thus change its value; but how conceivably can you change the value without first changing the degree of the demand? The underlying conception throughout the whole of the mathematical and semi-mathematical economics is, however, just this, that supply, in some unexplainable fashion, acts continually on value without the intervention of any action on demand. Professor Pigou, for example, in dealing with the subject of wage fluctuations, tells us that 'a perpetually fluctuating wage' is the sort of wage that 'pure theory recommends.'[1] When we listen to such an argument, we recognise that the reasoner seems to think of the relation between supply and price in the light of the action of a physical force on a material body, it might be as the relation between the force of the wind and the motion of the ship. Just as the constantly varying strain of the wind on the sails is immediately translated into variations in the speed at which the vessel cuts the water, so supply is supposed to exercise a constantly varying influence on market value, causing it to shrink in precise proportion to its increases, and to expand in precise proportion to its decreases.

Human Recognition omitted.—Such a conception, however, plainly fails to reckon with one great and obvious truth, the truth, namely, that changes in supply can produce no effect whatever upon price apart from human recognition of their existence. Suppose that the supply of raw cotton, for example, was, as a matter of fact, being rapidly and

[1] *Principles of Industrial Peace*, p. 75.

steadily augmented in some out-of-the-way corner of the world, while we in Europe knew nothing about the augmentation; manifestly enough this increase of supply would be all the while producing no effect whatever on prices here. They would go on just as if it did not exist. Suddenly, however, intelligence respecting it might reach us, and then the price of cotton would fall probably by dozens of points at a bound.

Infinitesimals.—A great point is made, especially by the most ultra-mathematical of the mathematical theorists, of the effect on price of infinitesimal increments of supply. A man who does not know all about infinitesimals is supposed to be altogether incapable of dealing with the more complex questions of economics. What is forgotten, however, is this, that infinitesimal increments are below the threshold of consciousness, and cannot conceivably take any effect on price whatever. It is only when there are enough of them accumulated to become quite palpably recognisable that they can begin for the economist to exist in any sense. Let us once reflect that there is fundamentally only one way in which increase of supply can lower prices, that is, by making each potential seller dread being left with his product on his hands, and we will then realise that a man might just as reasonably set himself to say his prayers by machinery as attempt to apply mechanical methods to the exposition of what are in truth the phenomena of life and mind.

The Law of Diminishing Utility.—The application of the Law of Diminishing Utility, as it is called, to the explanation of the processes by which prices are determined, assumes, of course, the direct action of supply on value. The theorist takes the simple barter transaction as adequately representing the process of exchange in the commerce of to-day. One man has a stock of bread which is undergoing a steady process of augmentation; another has a stock of sugar of which the same may be said. Finally, the growing satiation of each that accompanies the increase of his own commodity attains a degree of intensity which

makes him desire to exchange some of it for some of his neighbour's commodity, and the exchange accordingly takes place. Who is not familiar with it all now *ad nauseam*? This is presented as a type of commercial transactions generally, and it is on this presentation that the curve theory rests. As there may be said to be at any moment a definite proportion existing between the amount of food consumed and the intensity of the unsatisfied hunger that remains so, it is held, there is always some special price that is appropriate to each varying amount of each commodity that is in the market.[1] With increasing supply this price is represented as descending regularly from point to point, tracing as it does a curve as smoothly continuous as the parabola traced by a stone thrown into the air.

Let us concentrate attention for a moment on what is here represented as being the universal cause of exchange. The reason why any man parts with a portion of any commodity which he possesses lies, it is made to appear, simply in the fact that he has more of it than he can use himself or, at any rate, than he cares to use. This being so, we must conclude that when we find Messrs. Harrods or Messrs. Whiteleys selling blouses and coats and skirts at the present moment, the reason why they are doing so is that they have got so many of them that they really cannot use them all themselves. But why, again, did they buy them? According to the theorists, at the time they bought them, their 'marginal utility' or 'desireableness' must have loomed so large in their eyes that they were literally impelled to part with something in exchange for them, and so they parted with the purchase money. Could any explanation of an economic fact be more farcically absurd? The marginalists are, of course, here in the throes of their life-long struggle, by hook or by crook, to appear, somehow or other, to be dealing with commercial transactions in non-monetary terms.

Let us try to get at the rights of the case. Why, as a matter of fact, is it that Harrods are to be found at the present moment selling blouses and coats and skirts?

[1] Marshall, *op. cit.* See eq., p. 283.

Common-sense answers ; simply because they bought them a week ago, or a month ago, with the intention of selling them. Their thought in buying them had, of course, nothing to do with the desireableness of such things from their own point of view, or that of their families. They looked at the whole transaction from start to finish as a unit, and hoped that its net result would be to leave them with more of the monetary substance in their hands or at their immediate command than they had before. That was their aim, their intention, what they wanted. All that was conative in their psychology at the moment concentrated itself round this one point, the securing of the largest possible profit in money from the transaction as a whole. Desire in the matter was not a perpetually fluctuating factor as represented, but, on the contrary, was a constant. Conation in no sense whatever bore directly on the coats and skirts or the blouses. They were mere intermediaries ; their purchase and their sale alike were mere means towards an ulterior end. They were the subjects, no doubt, of thought and calculation, but not of desire. The representation, as regards the whole sphere of business and commerce at any rate, that the waxing and waning desire for the things interchanged, on the part of the interchangers, has anything to do with causing or stimulating the sale and the purchase of them is thus seen plainly enough to have no sort of validity about it.

The idea that money is only wanted for the things that it will buy contains, at any rate, as much falsehood as truth. Many of us want it for the consideration that its possession directly confers. Passing over that point, however, let us, for the moment, keep in view the case only of those who do want money for the things they can buy with it, there is still all the difference in the world between aiming at getting things directly, and aiming at getting the thing by which anything whatever that we please can, at some future date, be commanded. In the latter case there is no definite ultimate thing that is the object of our pursuit. The sole nameable or realisable object is the intermediary. Suppose that that intermediary were electrical power developed

to such an incredible degree that it would, unassisted, provide us with everything that we could wish for, that it would transport us to the ends of the earth, and would even defend us from enemies and dangers of all sorts. We should all give up working to acquire special objects, or to attain special ends. We should all concentrate all our efforts on acquiring the maximum amount of this electrical power. Put the monetary substance in the place of such power, and the thought may assist us to realise what, as a matter of fact, happened in the world when one substance first established itself as the standard. Under modern conditions, the acquirement of special commodities, except as a means to obtaining money, is practically an end in life with no one. Whatever one may want one seeks to obtain by the roundabout process of getting the money that will command it, rarely indeed by the direct attempt to make it or procure it. To ignore the fact that the roundabout process has been substituted in the world for the direct is the strange achievement of the Austro-English school with their Law of Diminishing Utility, and its supposed translatability into terms of price.

The Fallacy of Identical Variation.—Before leaving the mechanical conception of value, it will be worth while to present some other illustrations of its working, culled from the writings of the most authoritative of the theorists, Professor Marshall.

The conception of smoothness and regularity as characterising the curves that represent concurrently increase of supply and decrease of price, or the reverse, assumes, of course, some sort of concomitance of variation between the two. It seems, indeed, at first sight at any rate, to postulate the assertion that if you halve the supply, you will double the price, and so on. This gross form of the assumption has, however, been a dozen times refuted. Mill, for example, following Tooke, points out that a deficiency of one-sixth in the wheat crop may cause a rise of a hundred per cent. in the price of bread. It is a little surprising, therefore, to find Professor Marshall remarking that ‘ If

now a new invention *double*[1] the efficiency of work in any trade, so that a man can make *twice*[2] as many things of a certain kind in a year without requiring additional appliances, then these things will fall to *half*[3] their old exchange value.'[4]

The false assumption is evidently a veritable John Barleycorn for vitality. In spite, indeed, of Mill's refutation of it, his own doctrine of the effect of an increase of money on prices in a community is manifestly pervaded by it in every line. We may name it the fallacy of identical variation.

Marshall on the Elasticity of Demand.—The false reasoning, however, ordinarily takes on a subtler form, and appears perhaps not as the assertion that doubling the supply will halve the price, or that doubling the price will halve the demand, but that some other definite proportion, say that of $2\frac{1}{2}$ to 1 will, in given circumstances, be found to hold good between the two. That is the view that presents itself under the heading of the Elasticity of Demand. 'Speaking more exactly,' Marshall remarks, 'we may say that the elasticity of demand is one, if a fall of 1 per cent. in price will make an increase of 1 per cent. in the amount demanded; that it is $2\frac{1}{2}$ if a fall of 1 per cent. in price makes an increase of $2\frac{1}{2}$ per cent. respectively in the amount demanded; and so on.'[5] The writer, as his accompanying diagram very clearly shows, makes the perfectly gratuitous, and, indeed, altogether false assumption that if when the price stands, say, at 10s., a fall of 1s. will produce a certain effect on the amount demanded, the same degree of fall will produce a precisely similar effect when the price stands at 9s., 8s., 7s., and so on. Without some such assumption, indeed, the application of the curves is manifestly impossible.

Leaving that point, however, let us inquire whether, generally speaking, the doctrine has any sort of vestige of foundation. 'The elasticity of demand in the market,' we are told, 'is great or small according as the amount

[1] Italics mine. [2] Italics mine. [3] Italics mine.
[4] *Op. cit.*, p. 511. [5] *Ibid.*, 102 *n.*

demanded increases much or little for a given fall in price, and diminishes much or little for a given rise in price.' [1] The principle is thus laid down that 'when demand is elastic for a fall in price, it is elastic also for a rise'; that is to say, that whenever demand expands readily and much on a fall, it will contract similarly on a rise. Is there, however, any truth whatever in this statement? What makes demand expand conspicuously on a fall in price? What can it be but the widely spread desire for a commodity in the community? But if that is the case, will not the existence of this very desire tend *to prevent the demand from contracting* in the event of a rise? Marshall himself points out that the greater the variety of uses of which commodities are susceptible, the greater will be the elasticity of demand for them. The fact of having various uses will, of course, make the demand for a commodity readily expand on a fall, but why should it make it contract on a rise more readily than would the demand for a commodity whose uses were less varied? Plainly its tendency would be precisely the opposite. Again, he instances things used for display as things for which the demand is very elastic. For them, as he says very truly, men's 'desire' is almost insatiable. But if that is so, surely the demand for them, though it may expand rapidly on a fall, will not contract with exceptional rapidity on a rise, and notoriously it does not. It may indeed, in such circumstances, be completely maintained, or even be increased in the face of the rise, especially if that rise, as often happens, should stamp the commodities in question as fashionable.

The absurdity of the use of 'elastic' as applicable to the case of contraction on a rise, may be judged from the fact that if the demand expands so that the same amount of the commodity continues to be bought after the rise as was being bought before it, it is then actually said to be 'inelastic.' Inelasticity is thus strangely used as a synonym for what Professor Sidgwick denominates 'extensibility.' What can be more evident than that this characteristic of elasticity, as here conceived and defined, can correspond

[1] *Op. cit.*, p. 102.

to nothing whatever in the world, for the simple reason that it embraces contradictory attributes ? The truth is that if we directly reverse the statement of the doctrine, we shall be much nearer the truth than if we accept it as it stands.[1]

[1] Professor Pigou, in his *Principles of Industrial Peace*, builds an elaborate structure of Euclid-like reasoning, illustrated by very complex diagrams, on Professor Marshall's definition, as above quoted, of the elasticity of demand. If the definition, however, will not hold water, how about the structure that rests on it ? As an example of the strange conclusions to which the thoroughgoing application of the mechanical system can lead a highly competent reasoner, we have Marshall's conclusion set forth in a note to page 467 of the work so often cited, to the effect that 'If a given aggregate taxation has to be levied ruthlessly from any class, it will cause less loss of consumer's surplus if levied on necessaries than if levied on comforts.' That is to say that if it were necessary to tax the poorest class in the community, they would feel it less if we taxed their bread and their milk than they would if we taxed their whisky, their tobacco, or their music-hall entertainments ! If any one is curious to know, more in detail, how this remarkable conclusion is arrived at, we must refer him to Marshall's thirteenth chapter of his fifth book, with its mathematical notes and diagrams.

CHAPTER VIII

THE DOCTRINE OF AUTOMATIC PRICE DETERMINATION

We shall have to revert to the subject of price determination at a later stage of our inquiries, after money and credit have been dealt with. In the meantime, however, it will be worth while to glance at the marginalist theory on the subject. It forms an integral part of the curve representation system, and must stand or fall along with it. In Marshall's exposition of the matter, buyers are represented as going into the market with a list of prices in their minds, at which they will take varying amounts of the commodity offered. A buyer, for example, is supposed to be willing to take 6 lb. of tea at 50d. per lb., 7 at 40d., 8 at 33d., and so on. This list is his 'Demand Schedule.' It can be represented by a regularly descending curve.[1] The sellers, at the same time, come to the sale, it is said, with lists of prices in their minds, at which they will sell varying amounts of their commodities. These lists are their 'Supply Schedules,' and these supply schedules also can be represented by regular curves. Where the curves intersect, that is to say, where buyers' and sellers' prices coincide, there a transaction will take place.

Edgeworth's Market Machine.—Professor Edgeworth, who, no doubt, stands less in awe of the common-sense of the plain man than most of his compeers, illustrates the operation of the principle as follows: 'You might suppose,' he says, 'each dealer to write down his *demand*, how much of an article he would take at each price, without attempting

[1] *Op. cit.*, p. 96. This, it will be seen, is a theory of prices which, strangely enough, takes prices for granted as in existence already. This aspect of the case will occupy our attention later on.

to conceal his requirements ; and those data having been furnished to a sort of market machine, the price to be passionlessly evaluated.' [1] If, however, this is anything like a correct description of what happens, or of what could conceivably happen at an auction sale, then how could it ever be possible either for buyers or for sellers to change their minds by a hair'sbreadth as to what they will give, or to what they will take while a sale is still going on. If they might be supposed thus to change their minds indeed, there could be no pretence manifestly of representing market phenomena by regular curves.

Well may M. Yves Guyot say that these theorists represent men as automata.[2] Men are not automata, however, and, as every one knows, at auction sales in the real world prices dart up and down in the most unexpected and incomprehensible fashion. Say that the sale in question is a sale of sheep. You look in at one o'clock, perhaps, and see a pen of wethers off the shears selling for 12s. per head.[3] You look in again half an hour later and see similar sheep selling for 14s., while, perhaps, by the end of the sale, sheep just as good have to be taken home unsold, though their owners would have willingly accepted 11s. for them. You think, perhaps, that some news must, in the meantime, have come in from the outside world with regard to market prospects ; first, perhaps, good news and then bad. Nothing of the kind ; the progress of the sale itself furnishes the facts which cause the fluctuations of price. Some of the buyers, guided by previous experience, have, it may be, a vague price limit in their minds when they come to the sale. Others, the majority probably, so far from coming there with any pre-determined 'Demand Schedule,' come intending to watch how things go before making any offer whatever. They see, perhaps, pen after pen taken up at prices that surprise them. Then, fearing that they may not get what they want at all, they, too, bid, and so drive prices higher yet. Presently, a large amount of demand being satisfied, there is a lull. Sellers, then, in their turn,

[1] *Mathematical Psychics*, p. 30. [2] *La Science Economique*, p. 106.
[3] The conditions before my mind are New Zealand ones.

begin to be afraid that they may have to take their stock home unsold, and so lower prices are accepted. Demand and supply thus, it will be seen, are far more closely interlocked than is assumed by the mathematical theory. Indeed, the very same position of matters as regards the quantity sold and the quantity that remains, may present itself to one man as increased demand, and to another, or to the same man next moment, as decreased supply. One man, too, may be altogether differently affected from another by the very same price fluctuation. A fall, say, takes place. It may be that buyers will say to themselves : This brings the commodity, whatever it is, within our reach, and so will absorb the supply ; or they may say to themselves, on the other hand, ' This fall is probably only the precursor of a further fall,' and so they will hold off, and prices will go lower still. How is any one to draw curves that will keep pace with mental processes so elusive and so unpredictable.

The conception indeed, as we have seen, of Demand and Supply as two co-ordinate but separated forces, each acting steadily on its own lines, and consequently capable of being represented by curves that intersect at a given point is one that is wholly devoid of foundation. There is, on the contrary, no single moment during the progress of any transaction in the market when the fluctuations of supply, as learned or as guessed at by the buyers, are not modifying the conditions of demand, and conversely, there is no moment in which the fluctuations of demand as guessed at by sellers are not modifying the conditions of supply.

A Rise in Price may increase Demand.—If there were any truth in the notion that as price falls, demand necessarily increases in some regular and calculable manner, and that as price rises demand similarly contracts, how could it happen as it does continually, that a rise in price becomes actually the *causa causans* of a further rise, and that a fall becomes often similarly the literal cause of a further fall. This can only come about because the initial

rise, instead of making demand contract, stimulates it, and because the initial fall, instead of stimulating demand, causes it to slacken and fall yet further.

A rise can become the cause of a further rise in very varying circumstances. There is the common case in which the lookers-on hear some well-known buyer raising his bids and follow suit. That, the theorists will probably tell us, represents a mere eddy that science may neglect. This neglect indeed of what they choose to regard as exceptional is a too prominent characteristic of their system. Here, however, is a case of another description. Say that the market that we are concerned with is the market for American Railway shares. Let us suppose that Union Pacifics, the price of which has ruled in the neighbourhood of 150 dollars, go up to 160 dollars. Every one who owns any of that stock at once finds both his realisable wealth, and his borrowing power considerably increased. A large number of such people, we may suppose, as indeed in fact continually happens, use this increased command of money to buy other railway shares, Southern Pacifics, let us say, Louisvilles and Pennsylvanias. The owners of all these stocks in their turn find their resources increased, and use some of their fresh wealth to buy, among other things, Union Pacifics, and so this stock again mounts further, perhaps to 170 dollars. It at once, of course, again reacts on every other stock, and sends them all higher. So the game goes merrily along till the whole list register a gain, it may be of 25 per cent. Thus we see that the initial rise in Union Pacifics, instead of being at once attended by a shrinkage in the demand for it, as the theorists tell us should be the case, has become the actual cause of a further rise, not only in other stocks, but in the end, in itself also. Of course, when figures like these above cited by way of illustration are recorded, the pace will probably be found to be too fast and furious to last, and a collapse will follow. The very same principle, however, which, in such a case, is seen acting in a wild and exaggerated fashion, acts in other cases in a more gradual and reasonable one. It is indeed very general and very far-reaching in its operation. If

we wish to understand the nature of any general rise of prices in a country, extending perhaps over a series of years, we cannot neglect the fact that whenever there is a rise in the value of any stock, or of any commodity, that rise is necessarily followed by an increase in the purchasing power over everything else exercisable by the owners of that stock, or that commodity. Once this increased power begins to be exercised, its tendency must be infallibly to make other commodities go higher. Cotton goods rise. Machinery, pig iron, wages of labour, perhaps, follow suit, and their rise causes a further rise in cotton goods. Theoretically the wonder is that the 'pyramiding' process ever stops. At any rate, though the tendency may in the end be overborne by other influences, it is always there as a *vera causa* to be reckoned with; and the fact of its existence is calculated to impress upon us a sense of the infinite complexity of the true sources of price fluctuations, together with a sense of the absurdity of supposing that they can all be embraced under one or two abstract formulas.

Perhaps the most important case, however, in which a rise in prices belies the formulas of the theorists by causing an increase of demand instead of a diminution of it, remains yet to be discussed. To understand aright the manner in which supply is capable of reacting on demand, we should think of it not as supply to isolated individuals, but as supply to nations or to groups. Keeping this in mind, we will find that we can hardly open our newspaper any morning without being struck by the manner in which the supply of Dreadnoughts, submarines, aeroplanes, and so on, to one nation stimulates the demand for them on the part of other nations. The first effect of the supply of a Dreadnought to ourselves is no doubt to satiate the existing demand for it, and this is the only effect of which the curve theory can take cognisance. The second effect is to be found in the demand that at once springs up in Germany for Dreadnoughts also, and the fresh demand for them that that fact again generates among ourselves. The same thing applies to some extent to all the expenditure that the regard to appearance has a share in instigating. Where it is present,

there, in forms more or less disguised, is the influence of rivalry with our neighbours present also. If a society woman thinks it necessary to appear in a new frock at each dinner-party that she attends, though they come about five times a week, there can be no question that the stimulus to the demand for dress in her case is the desire of outshining her friends. Her case is what might be called a predominant instance. It is true, at the same time, that the purchase of the most modest outfit in which any of us, or any of our wives or daughters are content to appear in the street has not been altogether free from the influence of the emulative instinct. We may not think of outshining our neighbours. It is quite good enough for most of us not to be conspicuously outshone by them. The desire not to be so is nothing else but the desire of living up to a certain standard which plays so great a part in modern economics. In our dress, our housing, and in everything on which we spend our incomes there is always, in our thoughts, some more or less veiled reference to the manner in which our neighbours are dressed and housed and live generally. The universality of the reference is at bottom the reason for the fact that supply, as it increases and takes new forms so constantly makes demand increase along with it.

In economic theory the fact seems to have been overlooked that scarcity demand in the case of such things as silks or jewels is something altogether different in its nature and origin from scarcity demand in the case of such things as wheat. In the first case scarcity appears to be the actual cause of the desire for the object which is desired, and consequently bought. In the second it is not. Wheat would always be wanted in, at any rate, as great quantities as it is wanted now, though it became as plentiful as water. If jewelry of any sort, on the contrary, should become so plentiful that the beach was strewn with it, no one would take the trouble to pick it up. Unaided by utility, beauty, or attractiveness of any sort, scarcity alone is capable of conferring on objects immensely high exchange value. Can any one imagine anything with less beauty, utility, or other attractiveness than a used Mauritius postage stamp

with a printer's error in it ? Yet scarcity alone has raised the value of such stamps to the figure of £1400 apiece, and will probably raise it higher yet. What is the secret of this singular phenomenon ? It can be nothing else but this, that the possession of a thing so scarce confers some degree of distinction on the possessor, and that the desire of such distinction is the most universal in its scope of all the desires that Nature has implanted in the human mind. In the modern economic world scarcity and high price are synonymous. So it comes about that a rise in price is often not only the precursor, but also the literal cause of yet further rises.

The Determination of Price in the Wholesale Trade.— There is yet another reason in addition to those noticed, why the teaching based on ' the translation of the law of Diminishing Utility into terms of price,' together with the diagrams that accompany it, fails to give us anything like a recognisable picture of what happens in the markets under modern conditions. It is this ; that what really takes place in two stages is represented as taking place in one. The simple barter transaction is taken as the type of commercial exchanges generally. The discussions of the last chapter will perhaps have made it clear, to those of my readers to whom it was not clear already, that what is said to happen in such a case, has, at any rate, not the remotest resemblance to that which happens in the case of business expenditure, to the purchases and sales made in the course of dealing and production. Is the theory then any truer as applied to the expenditure of consumption ? Undoubtedly it is to consumptive expenditure, in the main, that the theorists apply their reasoning and their diagrams. It is plainly consumptive expenditure, and it alone that is runing in their thoughts when they dwell on the resemblance between the satiation of demand in the markets and the satiation of nunger in the individual. We have seen, however, that even as regards it the curves cannot be made to represent price changes as they really are. The fact that a rise in price, instead of causing demand to contract, may

stimulate it, and that a fall, instead of stimulating it, may diminish or destroy it, is alone sufficient to establish that conclusion.

It is further important, however, to notice that, under modern conditions, ultimate consumers' demand does not of itself complete the process of price determination. If we regard price determination as the goal, that description of demand only takes us half way towards it, and then leaves us. The remaining half of the process is carried out by another agency altogether, the deliberate action of the wholesale dealers.

Take cotton goods, for example. We see existing stocks distributed through the retail shops of the country, passing gradually into consumption, and being again gradually replenished. Suppose that, in these circumstances, a change in the conditions of consumption takes place ; that brisker trade, perhaps, and better times set in. Ultimate consumers' demand will absorb the stocks more rapidly than before. That is, however, all that it will do. It will not of itself, on any important scale at any rate, automatically alter prices. Prices in the world, nowadays, as Mr. Bagehot remarks,[1] and, indeed, as we all know, are altered almost exclusively in the wholesale trade. The retail trader takes them as he finds them, and adds a fixed percentage. Their alteration will be effected by thought, by calculation, and by deliberate action on the part of the manufacturers and the wholesale men, and to such processes of thought, calculations and deliberate action the curves and diagrams can have no sort or semblance of application.

[1] *Lombard Street*, p. 138.

CHAPTER IX

THE MEANING AND THE MEASUREMENT OF VALUE

In the chapters that follow the present one, I propose to deal with Money and Credit. The present one may therefore usefully be devoted to the setting forth of some miscellaneous considerations in regard to the theory of value generally which will bring to a close the treatment of the more abstract part of our subject.

Supply as Substitution.—I had occasion in the last chapter to call in question the validity of the current conception of the relations of demand and supply to value, as co-ordinate forces acting on it similarly, though in opposite directions. Yet another aspect of the relation of supply to value calls for some remark. When we say that value falls or tends to fall, as supply increases, what we have before our minds is the homogeneous substance. Individual isolated objects, however, have value just as truly as homogeneous substances. How then does increase or decrease of supply bear on them ? My pony, Fido, for example, is worth, say, £30, but the supply of him stands on his four legs, and not even a miracle could either increase or diminish it. The consideration of such a case brings home to us the truth that the relation of supply to value rests on a more elementary fact than itself ; it rests on the relative facility or difficulty of substitution for the object valued either of a precisely similar object, or of one that will serve the same purpose. To revert to the case of the pony : if, owing to some change in market conditions, other ponies as good as Fido should come to be readily obtainable at £20 apiece, then certainly his value will fall to £20 like theirs. We can state the cause of the change in such a case either as being

the increased supply of ponies of a type like that of Fido, or the increased facility of substitution for him of other equally desirable ponies. The latter is, however, the more fundamental expression of the truth involved in the case.

Among the almost innumerable 'laws' which the mathematical economists have found and formulated, is one, the discovery of which is ascribed to the earliest and most eminent member of the school, Augustine Cournot. It is described as the 'Law of Economic Equivalents.'[1] It lays down the principle that as wood, for example, can serve as a substitute for coal, it is capable of affecting the value of coal. The new 'law' would tell us, if we did not know it already, that steam traffic can compete with horse traffic, or railways with canals. A similar, or, indeed, identical principle is frequently referred to by Professor Marshall as the 'Law of Substitution.' He confines his conception of its operation to the substitution that is possible between things of divergent nature, as, for example, the substitution of machinery for labour, or of electricity for steam power. The principle is, however, in truth quite universal in its scope. We have the possibility of substituting one sack of corn for another sack of corn quite as truly operative as an economic force as we have the possibility of substituting corn for meat, or horse-power for man-power. Thus viewed indeed, as we have seen, the fact furnishes us with the basic principle of supply. We can then introduce supply as one of the determinants of the value of an old master, or of a used stamp of a special issue. It is to the difficulty of finding perfect substitutes for such things that their high price is due; as it is to the extreme facility of finding a substitute, in ordinary circumstances, for any given cup of water that its monetary worthlessness is to be attributed. We need thus have no exceptional or necessarily negligible instances when we come to formulate our law of value.

When, again, we thus go behind supply, and regard the principle that underlies it, it becomes doubly clear that the conception which attributes to it a direct action on value, one that skips over and ignores its action on demand, is a

[1] Pantaleoni, *Pure Economics*, Eng. trans., p. 94.

false and misleading one. It becomes clear, too, that all the forms of the supposed inexplicable transmission of value, such as Boehm Bawerk's 'conduction' backwards of price into the costs that have long ceased to exist, or the prevalent conception of the operation of money on prices not through the play of economic forces at all, but by virtue of the simple 'augmentation of quantity' are mere chimeras, mere figments of the neo-scholastic brain.

Value in Exchange prior to Value in Use.—It appears to be very generally taken for granted that value in use, which represents the most abstract meaning of the word 'value,' is also its primary and fundamental one, and that its meaning as value in exchange is something that is merely secondary and derivative. Precisely the opposite of this appears to me to be the truth. The conception which etymologically underlies the meaning of the word is strength or efficiency; and it still at bottom retains that signification. We may compare with it the Greek use of δύναμαι in a similar connection. Aristotle seems always to think of the various values of different things as what they can do, or how far they will go in attaining their purpose, that purpose being no other than that of procuring, by way of exchange, the maximum amount of the monetary substance. That the natural trend of human thought has been from value in exchange to value in use, and not contrariwise, is in accordance with the analogy of other words of a similar character. 'Dear,' which began with the meaning of mere physical scarcity, as its connection with 'dearth' indicates, has come now to be applied to things and persons that are the objects of human affection. Esteem, which had once etymologically a connection with something so tangible as bronze,[1] has similarly assumed in the end a purely emotional signification. It would probably be found that something like this is the course which all words of the sort have travelled. The farther we go back in the history of races, the more concrete are the meanings of their words.

[1] The connection between *aes* and *aestimare* has, no doubt, been called in question. The best authorities still hold to it, however, M. Babelon, Professor Bréal, and M. Darmsteter among the number.

They begin with the physical and individual, and end with the psychological and the abstract.

It seems surely the most natural thing in the world, too, that anything which could by exchange procure for us a large amount of the monetary substance, and could thus put us in a position to satisfy any want whatever that the goods or services of other people could supply, should soon come to be regarded as the very type of all that is useful and desirable; and should thus, perhaps, come to be applied in the end even to those useful and desirable commodities which, owing to their abundance, do not possess exchange value. If this was the course of human thought in the matter, then the conception of strength or efficiency as the basic idea in value is explained; if it were not, then that fact seems altogether inexplicable. The thought of value in use or utility is, no doubt, in some sense, a more primordial one than the thought of value in exchange, but that fact is not to the point in connection with the course followed by the meanings of words. The expression of primordial meanings comes, as a rule, last, not first in the development of language. The most primitive languages, as we know, have no equivalent for the verb 'to be.' Wherever we look, however, in the sphere of thought and investigation, we find that the idea that the abstract takes priority over the concrete, that it somehow or other brings it into being and explains it, is still possessed of a grip over the academic mind that nothing can shake. It made Kant treat the Aristotelian categories, or a variation of them, as the psychological foundation of thought, instead of its last result. It is only in quite recent years that our educationalists have begun to discover that they were going the wrong way about their business in giving the precedence, in the teaching of language, to the rules of inflection and syntax over the living substance of human speech.[1] In the teaching of natural science, the same tendency has a remarkable monument yet standing in the *Introductory Science Primer*, by no less a hand than that of Professor Huxley, which begins the instruction of children under

[1] Though Locke pointed it out more than two hundred years ago.

twelve with a subtle, and for the most part, fallacious dissertation on the distinction between laws and causes. No doubt it is to this same tendency in human thinking that we have to attribute the fact that the economists, old and new, have so uniformly conceived it to be their business, in explaining value, to begin with the most generalised thought that the word embodies, imagining that they should be able thence to proceed without more ado to the explanation of the more concrete and individual aspects of its meaning.

Fanciful Measurements of Value: Boehm Bawerk.—In approaching the question of the measurement of value, it may be worth while at the outset to give a glance at the treatment accorded to the subject by the Marginalist and Austrian theorists. It illustrates, it may be said, in a striking manner the desperation of their endeavours to blend business economics with Crusoe economics, the monetary with the non-monetary point of view. Take the following, for example, from Professor von Boehm Bawerk. 'The value of a good,' he remarks, 'is *measured* [1] by its marginal utility'; [2] and, to illustrate the method of this so-called 'measurement,' he says that, 'The value of a good is measured by the importance of that concrete or partial want which is least urgent among the wants that are met from the available stock of similar goods.' That sounds like business. Has it, however—bitter experience forces us to ask—any real meaning? An illustrative example is given us. A man has two rolls of bread to last him out till he gets more. One he will eat. The other he will give to his dog. He now loses one of the rolls. What is the utility that he thereby loses? It is the 'marginal' utility, not the power or opportunity of feeding himself. That is attached to roll No. 1, which he still retains, but the power or opportunity only of feeding his dog, for the latter alone is dependent on roll No. 2 that is lost.

Suppose that all this is true, how can it seem anything but ludicrously irrelevant to the question of the *measure-*

[1] Italics mine. [2] *Positive Theory of Capital*, Eng. trans., p. 149.

ment of values. We have surely been engaged simply and solely with the play of motives in relation to human action, and not with the measurement of anything whatsoever in any sense. Generalise to the utmost the principle illustrated by the example, and the only conclusion that you can extract from it is the conclusion—whatever it is worth—that a man will satisfy his most urgent wants before those that are less urgent.[1]

The Same: J. B. Clark.—Take again Professor Clark's exposition of the doctrine. We come to an italicised cross-heading: 'This method of measuring wealth universal.'[2] The method referred to is practically what Marshall would describe as 'translating the Law of Diminishing Utility into terms of price.' Specimens enough have been given of it above. 'These principles,' he goes on to say, 'apply to the economy of a solitary islander of the Crusoe type as they do to that of a civilised society. A Crusoe does not need to measure values for purposes of exchange, but he has other reasons for measuring them. It is for his interest to use his own labour economically, and to that end he should not put too much of it into one occupation, and too little into another. When, by reason of a large store of wheat on hand, the specific importance of it is small . . . he should direct his labour to raising goats or building huts, where the utility of the increment of product to be gained is, for the time, greater.'[3] No doubt he should, but how any one can persuade himself that all this has anything to do with the measurement either of value, or of anything else, is almost beyond comprehension. It bears, of course, on the fact that a man, if he is fairly reasonable, will go on producing what is needed for the satisfaction of one future requirement until the claims of some other future requirement appeal to him more strongly. Similarly the bullock will spend the forenoon in grazing in his meadow, and will then turn to his pool for a drink. In the last case, as in

[1] Even this really means nothing more than that he will satisfy first those wants which he will be found, as a matter of fact, to have satisfied first. Cf. *Economic Method and Economic Fallacies*, pp. 103-109.

[2] *Essentials of Economic Theory*, p. 41. [3] *Ibid.*, p. 41-42.

the first, something is done, presumably not without a motive. In neither case is anything whatever measured.

One would think, when following such lines of reasoning, that the word 'to measure,' as applied to price and value, had no meaning that was not altogether vague and indefinite. We know, on the contrary, that the measurement of price and value can be almost as definite and precise as the measurement of weight by the balance, or of heat by the thermometer. In each of these latter cases, that which formerly corresponded only to a more or less vague subjective feeling, is rendered both exact and objective by its reduction to terms of spatial quantity, and very much the same thing happens with the measurement of price and of value.

The theorists follow up their assumption of the existence of measurement where, as we have seen, the thought of measurement cannot conceivably come into play at all by the assumption of the existence of measured 'amounts' of 'marginal utility,' which again are said to be used to determine 'amounts' of value. 'The law which governs amount of value,' says Professor von Boehm Bawerk, 'may be put in the following very simple formula: The value of a good is determined by the amount of its marginal utility. This proposition is the keystone of our theory of value.' Now, whatever marginal utility may be, it certainly is, as Dr. Davenport very well observes, 'a matter of the individual psychology.'[1] But matters of the individual psychology do not exist in measured or measurable amounts. One might as well talk of measured amounts of joy, or hope, or the sense of humour. We look, in short, for tangible meaning, and the theory offers us empty sound.

True Measurement implies a Measure.—Contrast, for a moment, with this hazy and elusive so-called measurement, the real and familiar measurement of prices and values in the actual world. This much, at any rate, at once becomes clear beyond all question, that we cannot have real measurement without a measure, and that this measure cannot be

[1] *Value and Distribution*, p. 312.

a mere phantasm of the mind. Nothing but a tangible material substance can possibly reduce the subjective to terms of objective spatial quantity. General Walker, in his exposition of the process of price measurement, takes it, as we know, for granted frankly and without any hesitation, that the existence in the community of 'one article of uniform quality which is susceptible of easy and exact division,' the standard substance, in fact, is a pre-requisite of any such measurement. There must also exist, of course, a 'general desire' for the possession of this substance. Granted these two facts, and there is then no difficulty in understanding how all commodities come to range themselves 'upon a scale of prices, the degrees of which shall be expressed in terms of this one article—money.'

As to the possibility of measured values in any sense without money, Jevons, indeed, tells us that in the state of barter, which the economists are fond of talking about, but to which, I think, nothing in the real world has ever corresponded, 'The price current would be a very complicated document.' Every commodity would have to be valued in terms of every other commodity. The thing, however, is palpably impossible. How could the thought of value ever be embodied in a definite figure, if value meant nothing more precise than a power of purchase over innumerable and ever-varying goods and services? No human mind could conceivably attach any meaning to such a thought.

The Anthropological Evidence.—This deductive conclusion finds abundant confirmation from even the most cursory glance at the anthropological evidence, at accounts of the state of things existing in the true moneyless world of to-day, the world where money has never yet come into being. To this we shall have occasion to refer more in detail later on, but will touch on some of its aspects now.

It will assist us, perhaps, to realise how it is that the monetary standard operates so as to make value objective, and thus, for the first time, measurable, if we take a glance at its mode of action in its rudimentary stages. The German traveller, Nachtigal, gives us an illuminating

glimpse of it just beginning to emerge in an African district. He had been travelling through moneyless regions, and found that in them he had to set about his necessary purchases furnished with a curious variety of commodities. He had to bring to market beads, cotton pieces, note-paper, sandal-wood, and many other things similar, and, for all that, he could never be certain of being able to buy what he wanted with any of them. Suppose that he needed a bushel of grain, he might think himself lucky if he could exchange a sheet of note-paper for an ounce of tobacco, the tobacco for a hen, and finally the hen for the bushel of grain. When he reached Bornu, he found that cowry shells would buy all that was offered in the market, and though, as he says, it was tedious enough to have to count out five thousand cowry shells as change for the Maria Theresa dollar, the improvement on the standardless condition was nevertheless immense.

The Objectivity of Value.—Such approximations to the thought of value as can exist in a pre-monetary state, must evidently be of a purely subjective character. Suppose you go into the primitive African market prepared to exchange beads for sandal-wood, sandal-wood for paper, paper for poultry, and so on, you will come away at the end of the day, if you have a good memory, with a large number of ratios in your head. You will, perhaps, note mentally for future guidance that for a sheet of note-paper you should get three green glass beads, and that for three green glass beads you should get a hen, and so on. But these remembered items are not yet prices. Your thought, 'I will let three beads go in exchange for a hen,' is one that has neither objectivity nor universality about it. It has not the effect of conferring any nameable characteristic either on hens, on beads, or on note-paper. When money emerges in any shape, the case is different. Instead of being able to say to yourself merely, 'I will exchange this bead for a string of cowry shells,' you may now say to yourself, perhaps, 'This bead should be worth a string of cowry shells,' while your sheet of note-paper being worth three

strings, is now thought of as being worth three times as much as the bead. Such a thought, simple as it seems, would have been impossible before the emergence of the cowry shell standard. That it is which first ranges the prices of all your commodities on one uniform scale. What the bead will fetch for you in cowry shells, moreover, it will fetch for any man, and this fact soon comes to be viewed as an attribute of the bead, one which we name its 'value.' Thus the gulf between man and man is bridged, a universally recognisable characteristic not previously thinkable is conferred on each item of your stock. Objective value at last springs into existence.

What then, essentially, is this objectivity? Without going deeply into the metaphysics of the question, it may be enough to say that a sufficient test of objectivity for our immediate purpose may be found in the answer to the question, whether the thing or the quality, that is the subject of discussion, is something that all sane persons are in agreement about, something indeed—in cases where the objectivity is perfect—that they cannot disagree about, no matter how polemical their dispositions. Take away the thermometer, and any two people may argue for ever about the temperature of the air in the room that they sit in. Bring it back, and further argument becomes impossible. In the first case we have subjective ungraduated warmth only. In the second we have warmth that is objective and graduated. What is it, in the case of value that corresponds to the first, and what is it that corresponds to the second?

We have arrived at the conclusion that what is measured when a price is fixed for anything is the power of the thing to procure for us the monetary substance, and that this power again depends on the strength of other people's demand for the thing in question. It may therefore be said that what is measured and graduated when prices are fixed is the strength of the outside demand.

The theory of value, however, is full of unseen dangers, and we soon find that we are getting on to thin ice if we attempt to follow out too unreservedly the analogy between

the measurement of physical forces by scientific instruments and the measurement of price and value in the course of commercial exchange.

In the first place, we have to face the fact that there are innumerable payments made every day that cannot be said, in any true sense, to measure anything at all. Nine thousand pounds were paid for the Leonardo-Lucas bust, but what, in the shape of value, could such a payment be said to have measured. I encounter, perhaps, a friend skilled in horseflesh, and buy from him a pony with 'three legs and a swinger,' at a price, say, of £50. What does the £50 measure? Not, certainly, the value of ponies. This is manifest enough. It is necessary, however, to emphasise it, as in practice the fact is by no means universally recognised. In the theory of Consumer's Rent, which plays so large a part in Marshall's system, not only are all actual payments supposed to measure values, but also all sorts of imaginary payments, payments that never were made, but that would, in other circumstances, have been made. Such measurements are described, moreover, as 'practical applications of the theory of value.'[1] They lead us into the economics of wonderland. By their application, as Professor Nicholson remarks, you may deduce the conclusion that 'the utility of an income of £100 a year is worth £1000 a year.'

If, however, it is not all sorts of payments that can be said to measure value, how, it may be asked, shall we distinguish those that do so from those that do not? The answer is this: Measurement of value emerges only when the price given for anything to-day serves as a guide more or less exact as to the price that will be given for the same thing, or a thing of similar character to-morrow, or at some future date. It emerges thus only when prediction becomes possible. The imaginary measurements of Consumer's Rent afford, of course, no ground for prediction of any sort.

Value Measurement and Physical Measurement.—We can see thus that while there is an important and interesting

[1] *Loc. cit.*, p. 133 *n.*

analogy between value measurement on the one hand, and the measurement of heat by the thermometer, or of weight by the balance, on the other, there are also great and salient differences between them. Weight and heat measurements are exact at once and for ever. Value measurement, on the contrary, varies continually in exactitude, and in certainty from one case to another. It is emphatically a thing of degree. At its maximum of certainty, however, it still fails to attain such definiteness as characterises the measurement of physical forces.

Value, after all, with all the apparent precision of which it is sometimes capable, belongs to the sphere of life and mind, and a natural law in that sphere, as I have endeavoured elsewhere to demonstrate, means something altogether different from a natural law in the inorganic world. In the latter it is always capable of affording a basis for perfectly precise calculation, in the former never. 'We can say of such natural kinds as silver or mercury, that at certain precise temperatures, and under certain precise pressures, they will be solid or liquid, or vapour. Of such a natural kind as Man, all that we can say with even approximate certainty is, perhaps, that he will not be born with his head between his shoulders, or that if his parents are pure-blooded whites, he will not be born black. At any rate, definite statements with regard to him can only be made definite by being made negative. No definite positive statement in the way of prediction in regard to him will ever be necessarily valid.' [1]

A comparison between the measurement of physical forces, and such measurement as is possible in the case of value, confirms and illustrates this general view. Measurement, in its primary and typical sense, depends upon the possibility of superposition. A foot-rule, for instance, can measure another foot-rule at one coup, or can measure a stick a yard long in three instalments. In such simple cases as this, we see at once that the possibility of measurement depends upon the existence of two measurable things,

[1] *Economic Method and Economic Fallacies*, by the present writer, p. 50. See also 'Causation: its Alleged Universality,' *Mind*, January 1896.

and that these two things, in order that they should be measurable, must be possessed of some degree, at any rate, of constancy of size and form. In a world where the size and form of everything were always in a state of flux, there could certainly be no such thing as measurement at all.

In regard to subsequent extensions of the meaning of the word, it will always be found that there is in them the implication of something that corresponds more or less perfectly to this constancy of size and form on the part both of the measure and of the thing measured. By the substitution of sight, and, subsequently, of mathematical reasoning for touch, the principles of superposition are capable of being extended to the vast measurements of astronomy. In regard to all of them, the necessity of the two constant measurables is as obvious as it is in the case of superposition itself. A more interesting extension of meaning is, of course, that which takes place when an invisible and intangible force is said to be measured by the use of a scientific instrument. Take the most simple of all such instruments, the balance, and let us suppose that by means of it we learn that a piece of gold will be balanced by just nineteen times its own bulk of water. On the strength of this discovery, we set the specific gravity of gold down without more ado, precisely at nineteen. We can only do this because we are able to assume without any hesitation, that the nature of gold and of water and of the balance are such that what has happened once will, in the same conditions of temperature and pressure, repeat itself with perfect precision. All the other measurements of physical science share in this character of calculable repeatability and of consequent exactitude. When we come to the measurements of value, however, we find at once that we are called upon to deal with a subject matter of a very different nature. The repeatability of the force to be measured is not indeed altogether absent, but it is to a very great degree modified.

Let us suppose that 100,000 quarters of wheat were sold yesterday in a world market like that of Liverpool at 38s. a quarter, we can base on that fact the conclusion that in

all probability to-morrow's price, and even the price of a week or a fortnight hence for wheat will not vary very greatly from that figure. Even as regards this conclusion, however, there is no certainty. News, of course, may come at any moment that will send the price either up or down by several shillings at a bound. The farther, too, that we recede from the date of the price that forms the basis of our calculations, the less exact and the less trustworthy is the guidance that it affords. The measurement of physical forces has, of course, nothing in common with all this. Archimedes, when he weighed a piece of pure gold in water, and found that it lost just one nineteenth of its weight, did not need to hesitate in concluding that in all possible circumstances, and at all conceivable dates to the end of time, any other piece of pure gold would do exactly the same; and he could thus proceed to the conclusion that Hiero's crown, which did not do it, was not pure gold. In both the case of specific gravity, and in that of anticipated price or value, there is prediction, but manifestly of a widely different character in each. In the case of specific gravity, the prediction that was found possible was universal in its scope, as well as definite and precise to the fraction of a grain. In the case of value, on the contrary, the subject matter is so elusive that one is led to wonder that any clearly conceived attribute can be predicated of anything on the basis of it. Yet, of course, we know that value is predicated of innumerable commodities on the strength solely of this merely probable anticipation of events; and the fact that this happens is of enormous practical significance in the world. It has, for one thing, had the effect of conferring on commodities generally many of the characteristics of actual money, of making them, through the medium of bills of exchange and other such documents, the vehicles of purchasing power, and of thus enabling them to affect the prices of other commodities just as literal money would affect them.

In choosing as our illustration of the measurement of value a commodity in universal use, together with a world-wide market, we have chosen a case in which such calculable

repeatability as value possesses is at, or near, its maximum. Even as regards that case, however, we have seen how very different a characteristic it is from the calculable repeatability of physical forces; and the contrast appears in a still stronger light, of course, when we come to commodities that are subject to the fluctuations of fashion; and yet more again when we come to the things that we do not ordinarily think of as commodities at all, things such as houses, lands, and old masters. Value, it becomes more and more evident, cannot be regarded, like specific gravity, as truly representable by any one definite figure. What it is in truth is merely a limit of variations. Here, however, an illusory effect is introduced by the exigencies of practical life. In balance-sheets, for example, it is always found necessary, or at any rate convenient, to state values in definite single sums, with the well-understood proviso that the true value is something that we may expect to find more or less above or below them, but at any rate somewhere in their neighbourhood. The sum mentioned is rather to be regarded as the best representative available of the true value than as its literal expression. The exactness of the sum, however, fixes attention, while the tacit proviso is overlooked; and so value tends to come to be regarded as something that has the precision of mechanism, and of the forces of the inorganic world, instead of being regarded as characterised by the uncertainty and indefiniteness which rule universally in its own true sphere, the sphere of life and mind.

The confusion of thought thus generated is undoubtedly at the root of the idle fancy that questions of value can be usefully explained or illustrated by means of figures consisting of regular curves with intersections determined at mathematical points.

CHAPTER X

RECAPITULATION

It is time now to take a survey of the route over which we have travelled, and to summarise the most important of the conclusions at which we have arrived, not disdaining fresh illustrations if they present themselves.

Our initial chapters up to the end of the fourth—omitting the introductory one—were devoted to an inquiry into the nature of proof in economic theory. Such an inquiry is obviously a matter of elementary concern, and it might perhaps have been expected that most writers who approached the subject would have found themselves forced to devote some preliminary pages to it. So far, however, is that from being the case, that it would not be easy to point to any economist who has dealt with it in any shape or form. If the description of proof that is in this case applicable were on all fours with the usual methods of proof in physics the omission would be comprehensible, but that is evidently not the case. Economic proof is, indeed, much more closely analogous to the reasoning on the point of law in jurisprudence, a description of reasoning in regard to which our treatises on logic are unaccountably silent.

As regards proof in physics itself, a word or two may, with advantage, here be said. In spite of all that has been written about it, there is not such unanimity in regard to its nature as one might expect. Mill, still our most authoritative exponent of the subject, in the earlier part of his work, treats Induction and Deduction as two separate and co-ordinate varieties of reasoning. In a later chapter, that on Deduction, he, much more truly, concludes that every reasoning process must include both an induction, a ratiocination, and a verification, that is to say, a deduction.

The induction rightly conceived is, as Whewell, in substance, expresses it, 'the light that goes up,' the happy thought, the illuminating generalisation to which no methods are applicable. The deduction, on the contrary, is the process by which such generalisations are either confirmed or rejected.

To Kepler gazing at the sky through his telescope, and noting the successive positions of Mars, the thought occurs, 'If the orbit of the planet is elliptical, these positions would be accounted for.' The thought is attended by the thrill of discovery. As Emerson says, 'Generalisation is always an influx of Divinity into the mind; hence the thrill that attends it.' Induction thus has an æsthetic and emotional aspect of its own altogether unlike that of deduction. Next in order comes the process of verification. When, on the following night, we again find the astronomer surveying the sky, the conception of the elliptical orbit is before his mind. He says to himself, 'If my hypothesis is right, I shall find Mars at such and such a point at such and such a moment.' He finds it. His hypothesis is verified. Have we in the reasonings of economic theory anything that can be said to correspond first to the preliminary guess, the hypothesis, and next to the observed facts that verify it and convert it into established doctrine? I have endeavoured to show that in regard to such a question as that which bears on the meaning that may rightly be assigned to the word 'Capital,' we have as our hypothesis, our preliminary guess, some trial definition of the word, say the definition that 'Capital is wealth used in the production of fresh wealth.' There is but one conceivable method by which such a hypothesis, such a trial definition, can be verified and established, and that is by carrying it in our minds while we take note of the various uses of the word Capital as employed in the living speech of men engaged in the business of the world, and by inquiring whether it will, or will not, square with the use in such circumstances.

If that is so, however, then these uses are our facts with which every definition and every economic doctrine based on such definition must be made to correspond. We may,

therefore, at once, set down as an absurdity the method of procedure adopted by so many economists, that of starting with the assumption that they may use economic terms in any sense that they please so long as they use them consistently. We are forced, on the contrary, to fall back on Walker's principle, that 'there is but one permissible use of an economic term, and that is the right one,' its rightness or wrongness, according to my contention, being ascertainable by its accordance or non-accordance with business usage.

We may therefore further conclude, that no words or phrases can be available for the purposes of economic investigation which are not in use in the practical business of life, because in the case of such words and phrases we necessarily find ourselves at sea without a compass, we possess no means whatever of testing the question of their rightness or wrongness. This consideration alone would lead us to relegate at once and for ever to the shelf the vast literature of marginalism. 'Marginal utility,' 'marginal productivity,' and the like are certainly among the words and phrases that have no uses outside the text books of the universities.

When we subject them to a closer scrutiny, moreover, we find that the reasons why they can have no practical use are manifest enough. It is because the meanings that the theorists attempt to assign to them are meanings based on impossible assumptions. Marginal land, marginal doses of capital, marginal labourers, and so on, are freely and voluminously spoken of as if they were things as familiar to every one as lamp-posts or policemen. But if you ask the theorist to lay his finger on any piece of land, any dose of capital, or any labourer, that is at this moment marginal, you find at once that he cannot do it. To do it validly, indeed, in any given case, one would need, among other things, to know what next year's prices for all the products of industry would be. The pretence consequently, that we can have in the productivity of the marginal labourer some sort of criterion of what his receipts ought to be, is simply words without meaning. The criterion, at any rate,

is evidently enough, one that neither the economists themselves, nor any one else has ever been able to make any use of.

As to the conception of marginal utility as affording an explanation of the nature of value, we found that it was an absurdity generated by the blending of inconsistent points of view. Whatever utility is, this much is certain, that it is a permanent property of things, not a passing state. It is a power residing in things, and at any time exercisable, not the fact of its exercise at a given moment. The marginal utility of the theorists, however, is no permanent property, it is nothing but a transitory condition. It is intense one moment, when supply runs short, and vanishes to nothing the next, when supply becomes redundant. The difficulty and mystery of the theory is due, and due solely, to the idle attempt to express the fluctuating sentiments of the subject in terms of the permanent properties of the object, to use adjectives, in fact, when other people would use verbs. If an exercise were set requiring the candidate for honours to express the varying feelings towards each other which took possession successively of the minds of Horace, of Lydia, of Chloe, and of Calais the son of Ornitus, without the use of any words except such words as are ordinarily devoted to the expression of the *proprium* as opposed to the *accidens*, the net result might easily be an agglomeration of terminology that would be just as fascinating to the academic mind as the Austrian theory itself.

In another aspect, again, we find the blending of inconsistent points of view followed by mystery of expression and apparent profundity of thought. Marginal utility, we found, when we ran the conception to earth, was really nothing else but demand; Seligman, indeed, tells us that 'When we speak of marginal utility, we think of demand.' The question next arises, however: Whose demand? Our own, or that of the world outside us? To this question we found that the theory gives a double answer, and that the giving of this double answer was the very breath of life for it, the very secret of its existence. It had become, indeed, an unconscious fine art, as we saw, with the theorists to so construct every sentence that was put on paper that

the attribution of marginal utility could be read either as applicable to the isolated demand of the individual, which, no doubt, he would know all about, or to the demand of the outside world, of which *a priori* he would know nothing. By passing backwards and forwards between these two meanings, and by that means only could this 'marginal utility' be made to appear to afford an explanation of the inner nature of value.

We heard accordingly of amounts of marginal utility which corresponded with, and 'measured' value in given cases. When such 'measurement' was analysed, however, it became clear that the word measurement as applicable to it was altogether inappropriate. What was described as measurement was the mere play of motives common to man with the lower world. There is, of course, at the same time, we know, a real measurement of value in the world, a measurement which may be said to register the varying intensities of a force in terms of spatial quantity, analogous, more or less, to the registration of the varying intensities of heat by the thermometer, or of weight by the balance. The force that in the case of value was measured and graduated was the force of outside demand for commodities, not, of course, of our own demand, with which the theorists confuse it. Such measurement it was hardly necessary to say, implied the existence of a measure; and the measure in this case could be no elusive phantasm of the mind. It must evidently enough be a real and tangible thing that itself occupied space.

In glancing at the theory of price determination current among the economists whose views we have been criticising, we noted the fact that it appeared to begin in the middle of the problem to be solved. It started by asking the question what would happen if prices that stood at a given figure should chance either to rise or to fall, but, at the same time, it left both unasked and unanswered the more fundamental question, how they came to be placed at any figure at all to begin with; what they were, in fact, and how they came into existence. General Walker, so far as I am aware, stands alone among the economists in making an attempt,

at an explanation of price determination which does not, to start with, take prices for granted. Perhaps the most interesting aspect of his attempted solution lies in what it postulates. In his view, as we know, in order that price determination should be possible, it is necessary, in the first instance, that some one substance should have become the object of a universal desire in the community. The intensity and the general diffusion of this desire, moreover, has to be postulated as being such that 'the effort of every dealer' will be 'to obtain *as much as possible*' [1] of that commodity 'for each and every part of his stock'; and this will 'result in ranging all commodities according to the cost of replacing them upon a scale of prices, the degrees of which shall be expressed in terms of this one article—money.' [2]

We may well pause here for a moment to ask what is the assumption that underlies the assertion of the existence of such a desire. It is clear indeed that it could only have come into being after a state of things had supervened in the world in which practically every one had, from some cause or another, come to make the acquirement of the greatest possible amount of this one commodity, the goal of all, or nearly all, his efforts, from the cradle to the grave. Suppose that for a day, or half a day, people generally ceased to be possessed by this overwhelming, this insatiable desire for the one article in question, the whole machinery of price determination would necessarily at once be brought to a standstill. The desire is nothing less than the motive force that underlies all the processes of economic change, yet economic science is as yet, it seems, unawakened to the recognition even of the fact of its existence. It is remarkable, as regards many departments of thought, how much we can assume implicitly without ever explicitly recognising even in our own consciousness that any assumption has been made. Philosophy largely consists, as Hegel puts it, in forcing people to recognise what it is that they themselves have said and are saying,[3] in bringing nome to them the

[1] Italics mine.

[2] *Money, Trade, and Industry*, p. 38.

[3] *Logic, Quality*, chap. ii. C. c.

unseen implications of their own familiar assumptions. We direct our attention perhaps to some great historical development in human life, as, in this case, to the emergence of money, and yet never reflect upon the motive force that must have lain behind it, or ask if any force was needed. Similarly the sages of the Directory, as we know, had their ready-made religions in their pigeon holes, and were prepared to launch them on the world as substitutes for Christianity, but omitted to reflect that something analogous to 'being crucified and rising again the third day' was requisite as a preliminary to getting them accepted by mankind. In the following chapter I will submit some suggestions in regard to the manner in which, as it seems to me, Money and the desire for money originated in the world.

CHAPTER XI

THE ORIGIN OF MONEY FROM ORNAMENT

In every department of investigation science has long been busy with problems of origins. Wherever it has turned its activities, it has always been certain to find some variety of the anthropomorphic explanation in possession of the field. The rocks with their fossils, as we now find them, were thought to have been made in an hour by a wave of the Creator's hand. Human languages were supposed to have sprung full-fledged into existence at some definite date in the world's history. Civil government was believed to have been, likewise at some given date, established by a convention between king and people. These fantasies have now, of course, for the most part, been dissolved, mainly by the half-conscious change in our point of view that has accompanied advancing knowledge. In regard to one great social phenomenon, however—money—the case is different. There the conventional explanation is still usually looked upon as quite good enough. Mankind, we are told, having had experience during some generations of the inconveniences of the system of barter, fixed at last on some one substance which they should regard as their medium of exchange, and, having done so, eventually arranged that it should be impressed with the stamp of authority. This, in the fourth century B.C., was Aristotle's explanation of the phenomenon, as in the eighteenth century after Christ it was Adam Smith's, and as it still is that of our economists, with few, if any, exceptions. It is to this day to be found, either expressly set forth or tacitly taken for granted, practically in every treatise that deals with the subject.

To the trained ethnologist, one would think that merely

to put such a theory into words would be to refute it. Ethnology knows nothing of institutions that spring into existence all of a sudden, or without a long previous history of silent and hidden underground development, and rarely or never does it know anything of institutions whose origin has been in any sense the work of conscious intention. The ethnologists, however, in this country at any rate, for some reason that is not altogether obvious, have given little attention to the origin of money, and even in our books of travel, where the customs of primitive peoples are dealt with, references to its early development are few and far between.

Ridgeway : Babelon.—Besides ethnology and economics, the origin of money has been the concern of yet another science—numismatics. It is from the point of view of the numismatist, for example, that Professor Ridgeway, in his *Origin of Metallic Currency*, has approached the question, and his inquiries have, at any rate, been more fruitful than the conjectural history of the economists. A still more important book of the same class as Professor Ridgeway's is *Les Origines de la Monnaie*, by M. Babelon, the leading numismatist of France and of the world. Both these books are storehouses of interesting and suggestive facts in reference to the almost infinitely varied objects and substances that have, at one period or another, and in one country or another, assumed functions more or less analogous to those of our circulating medium.

Andrée.—In Germany, again, it is the ethnologists rather than the economists or numismatists who have dealt with the subject in an enlightening manner. A section in Richard Andrée's *Parallelen*, a book which deals with a great variety of ethnological questions, helped to lay the foundation for future advance by attempting a formal classification of the various kinds into which incipient money has to be divided. His classification is based mainly on the nature of the material used, the division being into such groups as stone money, shell money, salt money, etc. No answer was thought of or attempted to the one question

which goes to the heart of the discussion—the question, How did it come about that while almost everything that can be mentioned, from cattle and slaves to kitchen pots and kettles, and from salt and tea to shells and feathers, has at one time or another been used in the world more or less in the character of money, it is the precious metals that have finally ousted everything else from that position, and that hold it to this day?

Schurtz.—The absence of any answer, or attempted answer, to this question also characterises a more recent and greatly more important German contribution to the study of the subject, the *Grundriss einer Entstehungsgeschichte des Geldes*, of the late Dr. Heinrich Schurtz, of Bremen. He also frames a classification of early moneys ; but with him it must be said that the grouping is made on more philosophical principles. We find with him such classes as ornament money, utilities money, and clothes money, the first class being subdivided into the two groups of shell money and metallic money. He also then divides the whole series into the two great classes of money for use within the tribe and money for intertribal use,[1] and thinks that our modern money has been formed by the amalgamation of these two, and that it owes some of its salient features to each, very much, he thinks, as modern marriage owes its salient features in part to early exogamous, and in part to early endogamous relations. The attempt to follow out this somewhat fanciful parallel between the development of marriage and the development of money leads the writer, as it seems to me, off his track. His work for all that contains a great deal that is valuable and suggestive, and makes a real advance in the discussion of the subject. As a thorough ethnologist, Dr. Schurtz is penetrated with the conception of money as having arrived at its present condition by a process of gradual growth of some sort, at any rate, and he dismisses as an absurdity the notion of its establishment by a convention. The most valuable portions of his book are, to my mind, the chapters

[1] 'Binnengeld' and 'Aussengeld.'

on the development of 'Binnengeld,' the money for use within the tribe. Such a view as the following is very significant. Dr. Schurtz thinks that at a period when everything in the nature of food and shelter was the common property of the whole tribe, and when, consequently, exchange as regarded them was practically unknown, payments that subsequently developed into regulated taxes began to be made in the shape of gifts to the chiefs to propitiate their goodwill, and payments that subsequently developed into regulated fines also began to be made in the shape of indemnities to the injured, and to the relations of the slain. If this view holds good, then, of course, so far must it have been from being the case that money was an expedient invented to remedy the inconveniences of the barter system, that it seems rather to have been the case that incipient money preceded barter in the world, and that we see in its development the rise of the agency that proved itself in the end of all others the most potent in bringing about the dissolution of the older communism, and in substituting for it the system of private property and exchange.

The Double Function of Primitive Ornament.—When one has a problem before his mind, sometimes it happens that one stumbles on a fact or a suggestion that contributes to its solution, in the most unexpected quarter. In 1898 I was busy with the study of the Indian currency question, and went faithfully through the considerable mass of evidence that was given before Sir Henry Fowler's Committee. In answer to the 10857th question, I came across the following passage which, it struck me at once, had an interesting and important bearing on the origin of money. The witness was the late Mr. Romesh Dutt, C.I.E., a native gentleman who has, it may be said, made his mark in literature.[1] In reference to the vast amounts of money spent annually by the natives on silver ornaments, he was asked by one of the members of the Committee,[2] 'Would

[1] In his book, *The Lake of Palms*, an interesting sketch of Indian life, at pp. 3 and 28, Mr. Dutt introduces reflections on the use of ornaments as a reserve for contingencies similar to those quoted in the text.

[2] Mr. Campbell.

not the country have been benefited if that money had been employed instead of being allowed to lie idle ?' 'I do not think it lies idle,' replied Mr. Dutt, 'because it serves the purpose of ornament and savings bank.' 'As regards savings banks,' went on his interlocutor, 'is it not very much more economical and better to put your savings in some interest-bearing security than to tie it up in a bag ?' The reply was very much to the point. 'If an Indian cultivator,' said Mr. Dutt, 'had 200 or 300 rupees in the bank, it would disappear in the course of a year or so, but if it is in the shape of his women's ornaments, he will keep them until he is compelled by famine to part with them.'

The silver 'serves the double purpose of ornament and savings bank.' Mark the double function. Perhaps we have caught the transition of ornament into money in the very act of taking place. To the shrewd Scotch banker who put his questions to Mr. Dutt, the putting by of so much annually in the shape of savings seemed so completely a matter of course that it stood in need of no explanation. The question how it was that saving first became possible in the world is, nevertheless, a very real problem. Share and share alike was the unvarying rule among primitive mankind. The sentiment that enforced that rule, indeed, has survived with considerable vigour into the modern civilised period. There are, as we know, large classes among ourselves for whom social opinion makes saving practically impossible. Among races which belong to an earlier stage of development, the same sort of social opinion is infinitely more powerful. If the Indian peasant had his 200 or 300 rupees in hand, or under his immediate control, the exigencies of some matrimonial or funereal function might in a day run away with the half of it. If, on the contrary, these rupees are melted down and made to take the shape of ornaments for his women, ornaments which, among the Indian peasantry, are almost the sole index of social position, and which enable the whole family to hold up their heads among their neighbours, nothing but very urgent necessity will make him part with them. Thus the desire for orna-

ment first makes the accumulation of a reserve for use in utmost need possible. This is the first stage. Presently, no doubt, some degree of consciousness of the double purpose of his ornaments begins to enter into the thoughts of the peasant. Experience tells him that the possession of a store of bracelets and bangles has warded off starvation from himself and his family in the past, and the possibility of the recurrence of evil days forms a conscious reason in his mind for continually adding to his possessions in them. Thus, after a fashion, a circulation of ornaments seems to have preceded in the world the circulation of money. This fact, as it happens, has struck one of the most competent of our numismatists, Mr. Keary, in connection with the state of things prevailing in a very different age and country from present-day India. 'In Beda,' he says, in his introduction to the catalogue of English coins in the British Museum,[1] 'there are passages which seem to point to the circulation of ornaments as a sort of currency. For instance, when King Raedwald, king of the East Angles, was tempted by the threats and promises of Aethelfrid, King of Northumbria, to betray the fugitive Eadwine, his wife dissuaded him from the act of treachery, urging that "it would not become so great a king to sell for gold his excellent friend in his hour of need, and for the love of money [2] to lose his character for good faith, which was more precious than all ornaments."'[3] In the mind of Beda, *ornamenta* and *pecunia* were evidently very nearly one and the same thing. The armlets of the Anglo-Saxon nobles were made on a definite scale of weight and standard of purity, and apparently were also so made as to be easily divisible into portions of a definite weight. The *scillingas*, from which our word shilling is derived, were originally pieces cut, or broken off, from these armlets.[4] A 'ring-breaker' both in the Anglo-Saxon and Norse languages, came to be used in the sense of a distributor of treasures, and was a title specially accorded to princes whose open-handedness the minstrel desired to celebrate.

[1] P. x, footnote. [2] Pecunia. [3] Ornamenta.
[4] Keary, Introduction to *English Coins*, p. viii.

The Interchangeability of Plate and Coin.—It is only, indeed, in quite modern times that the divorce between the double purpose of the precious metals as ornament and as money has become as complete as we now find it. As recently as two or three hundred years ago plate was commonly converted into coin, and coin into plate, much as in modern India rupees were commonly converted into ornaments, and ornaments into rupees. The cost of manufacture was then looked on as a trifle that hardly had need to be considered. Jean Bodin refers to a saying current in his day, that 'in plate one loses nothing but the fashion.'[1] Lord Burleigh's will leaves his plate to be distributed by weight among the legatees as if it were so much bullion. This state of things, moreover, left its impress on the thought of the statesmen and economists of the period. There was then an intimate relation in the public mind between plate and money, which it is hard for us now to realise. Sir Dudley North, for instance, in assailing the policy of a law which forbade the use of plate in taverns, argues that 'if every one had plate in his house, the nation would be possessed of a solid fund in these metals, which all the world desires.'[2] A proclamation of Charles the Second describes the English nation as having been 'in former times renowned for its plenteous stock of money, and the magnificence of its plate,'[3] as if the two were about one and the same thing. A goldsmith's is a very different trade from a banker's nowadays. Then, however, the goldsmiths inevitably became the bankers of the community, and their receipts for the treasure handed over to them became the precursors of our modern banknotes. Go back a couple of thousand years in the world's history, and a similar state of things presents itself. At the outbreak of the Peloponnesian war, Pericles is found reckoning among the financial resources of Athens the vases of the temples, and the gold that could be stripped from the chryselephantine statue of Pallas.[4] It may be remembered, too, how the

[1] *Discours sur le rehaussement tant d'or que d'argent*, t. iii.
[2] *Discourses upon Trade* (Reprint, 1822), postscript, p. 3.
[3] Ruding, *Annals of Coinage*, vol. ii. p. 322. [4] Thucydides, ii. 13.

people of Aegestae deceived the Athenian ambassadors in regard to the extent of their resources by inviting them to a series of banquets at various houses, where a great display of gold and silver vessels was made, the vessels being really the same sent on from house to house. It reminds one of the manner in which, about half a century ago, some of the American banks deceived the Federal government in regard to the amount of their reserves by sending these reserves on their travels just ahead of the inspectors.

It is worthy of note, too, that the precious metals are not the only form of ornament that has played a great part as money in the world. We find a few traces still of shell money, for the most part in Africa, but few of us are aware how vast at one time was the region, and how extended was the period of its dominance. The remarkable fact confronts us that in Chinese the very words for wealth and shells are the same. There was evidently a time when, for a great section of mankind, the thought of the cowry shell stood for all that the thought of gold stands for with us to-day.

Is it possible, then, it may be asked, to give any reasons that account for the fact of the attainment of the monetary position by ornaments rather than by objects of utility? One answer to that question has already been suggested. We have found that in certain stages of development the use of ornaments is that which alone renders the accumulation of private wealth in any form possible. At a subsequent stage, again, the intervention of the religious impulse is found to bring with it a fresh stimulus to the quasi-monetary use of ornaments. Men's thoughts came to be turned not only to the adornment of their own persons, but also to the adornment of their divinities. Thus, Delphi accumulated its hoard of treasure, and was able occasionally to furnish State loans to communities that stood in favour with its priesthood. 'The gods,' as Curtius says, 'were the first capitalists of Greece.'[1] They were likewise the first capitalists of early Babylon. There, indeed, as we

[1] See article translated by Dr. Head in *Numismatic Chronicle*, N.S., x. p. 91.

can gather from the evidence of the tablets, the accumulated wealth in the temples played a very important part in the commercial life of the community. A man starting in business would naturally borrow the capital that he required from the treasury of the Sun God, as here he might obtain it from a bank or a lending agency.[1]

The Emergence of the Standard.—Adam Smith, in his account of the origin of money, makes the significant observation that in order to avoid the inconvenience of the barter system, the prudent man would always endeavour to have by him a stock of some one substance which he had reason to believe that no one would refuse in exchange for his produce. He does not explain, however, how it could come about that in the primeval state of things any man could reckon on being able to find such a substance. If, indeed, such a substance were within his reach, then plainly it would be money, already in a fairly well-developed stage. The very problem before us is to ascertain how it was that any one substance originally obtained such a position in the eyes of the community that no one would refuse it in exchange for his produce, no matter when or in what quantities it was offered. As Walker says, 'Money is a thing of degree,'[2] and 'anything may become money if it acquires a sufficient degree of acceptability.' The problem before us is the genesis of this 'acceptability.'

We can see, I think, without much difficulty that ornament has possibilities, at any rate as regards the attainment of 'acceptability,' which things that supply mere bodily needs have not. Take wheat, for example. If a man has as much as he could eat, and as much as he could store, he would take no more in exchange for any of his possessions. He would hardly take it as a free gift. Wheat is thus liable to glut, while ornament is, at any rate, not so necessarily. When supply is conceived of as being made to tribes and nations rather than to individuals, and when the article supplied is one that contributes to the success of the

[1] Sayce, *The Babylonians and Assyrians, Life and Customs*, p. 128.

[2] See *Money*, p. 407.

individual in his contests or rivalries with his fellows, an exception is found to the rule that demand must diminish as supply increases. On the contrary, we find that every increase of supply may come to be indissolubly linked with an equivalent increase of demand. Give one tribe of savages on a new continent muskets, and muskets at once become a life-and-death necessity to every neighbouring tribe. The zone of demand must widen with every extension of the zone of supply. Peaceful life, however, has its rivalries and contests as well as warlike. The reason why the savage wants ornaments is that he may outshine his neighbours, or, at any rate, that he may avoid being outshone by them. Life might be possible without such ornaments, but for him not a life that is worth living. If he would win for himself a wife, if he would gain the consideration of his fellows, then they are not to be done without, and the more of them he can get the better. Thus the desire for the attainment of distinction, or for the maintenance of position in life produces essentially the same effects at both ends of the scale. At the one it makes men crave for necklaces, bangles, and nose-rings ; at the other, for the power of drawing, at his pleasure, cheques for great sums of money—that is, in the ultimate analysis, for the immediate command of great quantities of gold.

Suppose, however, that we can see some reason why a material of ornament might attain the degree of acceptability needed to convert it into money, a second question presents itself, the question, What was it that caused the precious metals to distance all other forms of ornament in attaining such a position, and how has the value of gold become so unvarying as the whole business world always regards it as being ? Every form of ornament must have had the tendency towards changes of fashion to reckon with. How is it that this tendency was overcome to a great extent by both gold and silver, to begin with, and that the possibility of its ever affecting the monetary position of gold, at any rate, is never so much as thought of now ? Here, I think, comes in the influence of the other currently enumerated monetary characteristics—homogeneity, portability,

divisibility, and so on. It was not, of course, that a convention of miraculous savages ever said to themselves, 'These metals are homogeneous, portable, and divisible, therefore we will choose them as our medium of exchange.' Things do not happen in that way in this world of ours. We have rather to look to the fact that the possession of these characteristics would confer on the forms of ornament that possessed them some degree of added suitability for early payments, say, for gifts, ransoms,[1] indemnities, and such like; and that, again, this suitability for such payments—payments that brought with them, perhaps, increase of social power and influence, or deliverance from death for one's self, or those dearest to him—would again react on the subjective appreciation of the ornaments, and would both enhance and steady their estimation—their beauty even—in the eyes of the tribe. The enhanced estimation would, again, increase their suitability for payments, and so the two forces would continuously react on each other, perhaps throughout long ages. We have a parallel instance of such action and reaction in the case of the transformation of dialects into distinct and separate languages. We have there to take account of the fact that every change of dialect tends to modify the organ of speech, while, at the same time, every modification of the organ of speech tends to make the changes of dialect always more and more pronounced. The most important of the monetary characteristics is homogeneity. It is homogeneity that first renders anything like precise proportionment of payments to the quantity of goods or the importance of services possible, and thus, as it seems to me, first enables the conception of value in the economic sense to come into existence. It is, therefore, interesting to note that this characteristic of homogeneity was shared by the shell money, which in a great part of the world anticipated the rise of metallic money. One cowry shell being much like another, they could be, and were,

[1] In the *Iliad*, while trade was in the barter stage, stores of gold and brass were held for such purposes as ransoms. See, for instance, the supplications for mercy of Lycaon and Dolon to Achilles and Ulysses respectively.

ranged on strings of given length, or measured out in vessels of a given size, and could thus, like gold and silver after them, begin to exercise the functions both of media of exchange and of standards of value.

Ante-monetary Exchanges.—The emergence of the Standard, then, as we have seen, was something very different from the conscious adoption of a mere expedient for the facilitation of exchange. It profoundly modified human thought on all the subjects that we now call economic. The natural thought of the savage in regard to exchange, and all that pertains to it, is to begin with, wide apart indeed from the thought of the civilised man. The savage is, as Livingstone remarks, as much astounded by the operation of money when he first comes across it as he is by the operation of writing. When primitive peoples begin to trade with each other, what arises at first is what Dr. Schurtz aptly enough describes as the system of fixed exchanges.[1] Arrows begin to be exchanged for pottery, perhaps, and the idea at once establishes itself that arrows are the thing to buy pottery with, and pottery the thing to buy arrows with, but that neither of them have any appropriateness for exchange for anything else. The commissioners who were sent to the Andaman Islands by the Indian Government to settle the monetary system there, bought, shortly after their arrival, a hen from the natives for a British rupee, and could never afterwards buy a hen for anything else, even though they offered other articles and other types of rupees which were intrinsically more valuable, so rapidly did the customary price, or rather exchange equivalent, establish itself. A number of quaint and curious lists of these equivalents have thus come into existence, and are found ruling in various parts of the ante-monetary world. Coote, for example, in his little book on the Western Pacific, furnishes us with a specimen of such a list from the Island of Isabel.[2] It appeared that there ten cocoanuts equalled one string of white shell money;

[1] *Bestimmte Überlieferung, Grundriss*, p. 79.
[2] Coote, *The Western Pacific*, p. 146.

fifty dolphins' teeth equalled one well-grown woman, one bakika, or marble ring, equalled a young man of middle height, and so on. The originators of such a document are plainly some way off from our modern notions of value.

Coming to more advanced tribes, we find the bargain beginning to make its appearance and economic forces beginning in a hazy and undefined fashion to exert their influence. There is an advance observable in the definiteness of their action when the things exchanged happen to be homogeneous substances, with regard to which measurement was already understood. On reaching the lake regions of Central Africa, Burton found that one bushel of sea salt would exchange for one bushel of grain, or one bushel of cowry shells.[1] Later, the salt production was a failure, and the fact was not without its effect on the exchanges. The bushel of salt then came to exchange for two bushels of grain or two bushels of cowry shells. Such an instance, while it shows us demand and supply beginning to operate, points, at the same time, to the difficulties and limitations of the natural man's thought in apportioning the quantities of commodities in accordance with them. As the principle of the wheel which now seems to us self-evident was, as we know from the historical evidence, only arrived at by slow and difficult stages of progress, so the apportionment of commodities in exchange in such a manner as to make them bear some relation to demand and supply, had its misty and arduous beginnings, not easily to be realised by minds trained through many centuries by the operation of the monetary system.

The glance that we have given at the moneyless world should be calculated to impress on us a sense of the vastness and the depth of the gulf that separates the monetary and non-monetary spheres of thought, and to bring home to us the illegitimacy of those lines of thinking that attempt to treat the two as one. The truth is, that they belong to different periods of human evolution ; they are separated by years that are probably to be reckoned by scores of thousands. We have found the theorists insisting on dis-

[1] *The Lake Regions of Central Africa*, ii. pp. 402, 416.

cussing the mere play of motives in terms of the valuation of goods, but the play of motives belongs to all mankind, and is shared by mankind largely with the lower world; the valuation of goods, on the contrary, is confined to human civilisation of a relatively advanced type. The satiation of bodily appetites, and the play of motives generally are, of course, not altogether out of relation to the determination of prices by the operation of supply and demand. Neither, however, for that matter, are the cawing of rooks, and the gibbering of monkeys altogether out of relation to developed human language. No one, for all that, would think of treating these two as the same. No one would be likely to mix up investigations like Professor Garnier's into the monkey language with questions affecting the import of the Latin subjunctive, or the Greek use of the particle in *de*; or would expect the first class of inquiries to throw light upon the second. Yet the mixing up of things that are just as disparate as these, is an essential feature of all the 'Austrian' and mathematical theorising. The theorist, after setting forth the manner in which the imaginary Crusoe might be expected to act in providing food and shelter, will perhaps say lightly, as Professor von Boehm Bawerk, for example, does: 'Transfer now the field of illustration to the bustle of a highly organised economic community,'[1] or, as Professor Marshall puts it, 'Now, let us translate this law of diminishing utility into terms of price,'[2] unconscious, apparently, that what such a casual sentence seems to bridge is in reality untold millennia of life and progress.

[1] *Loc. cit.*, p. 152. [2] *Ibid.*, p. 94.

CHAPTER XII

EXTENDED MONEY. ITS BEARING ON PRICES

So far, in treating of money, we have taken it as being synonymous with metallic money. It is obvious, however, that, before we can deal adequately with the question of its bearing on prices and on economic problems generally, it will be necessary for us to inquire into the nature of that extended money which, through the agency of the banks, plays so conspicuous a part in the transactions of the present day. It will be worth while, to begin with, to give a glance at it in its historical aspect.

Historical.—As regards wholesale trade, the use of documentary money is both older and more widely spread in the world than the current view recognises. It is the application of credit documents to the purposes of retail trade that is more or less of a novelty. Rice Vaughan, writing in the Stuart period, notes the fact, in words that have quite a modern sound, that the Italians had developed their bill of exchange system to such an extent that they had almost succeeded in doing without metallic money altogether. Boisguillebert, about the same period, says something the same about the merchants of Lyons. Given once the possibility of transferring property by note of hand—itself, of course, a comparatively late development—and something analogous to our credit money seems inevitably to spring into existence. It existed apparently in a fairly developed form in Babylon and Assyria. Le Normant quotes the evidence of the tablets to show us that it had become quite usual for A in Babylon, say, who owed a certain sum of money to B in Ur,[1] to avoid the dangerous

[1] That is a certain weight of silver, as coinage was probably unknown. It is curious to reflect that bills of exchange and the like apparently preceded coinage in the world.

transit of the desert with silver in his possession by instructing, by letter, C in Ur, who was his debtor, or with whom he had money on deposit, to settle his account with B.

We sometimes hear the Bill of Exchange spoken of as the invention of the Jews in the Middle Ages, and the statement is currently made that it was entirely unknown in the Roman period. It is plain enough, however, that something practically indistinguishable from it existed then. Cicero, living in Rome, arranged to finance his son in Athens, by a letter of credit or some document of the sort. In the following, from the *Digest*, we seem to have a glimpse of a state of things in which the Bill of Exchange, or its equivalent, could hardly fail to come into existence. An imaginary case is put, in which 'Titius has a debtor in Carthage, and Gaius a debtor in Rome. Titius and Gaius agree that Titius shall collect and keep the debt in Rome, and Gaius shall collect and keep the debt in Carthage.' [1] If the agreement was put in writing, this writing would surely be something very like a bill of exchange. A question again is raised as to the validity of an agreement by stipulation on the parts of Titius and Gaius, that Gaius shall deliver the same day one hundred aurei at Carthage, the contract being made in Rome. Is such an agreement, it is asked, out of court, because it involves an impossibility? The answer is No. 'If each party had previously notified to his agent in Carthage that such a promise was to be made, there is no impossibility in the performance, and the stipulation is valid.[2] Here again we seem to see the Argentarii busy, like our own exchange bankers, with the settlement of debts between distant localities without the transfer of the metal.[3]

Justinian, indeed, says that the literal contract did not exist in his day, that is to say that, in his day, property could not be transferred by note of hand simply. We may

[1] D. 19, 5.5.4. [2] D. 45, 1.141.4.

[3] Even the days of grace appear to be of Roman origin. Perhaps we have the germ of them in the following: 'Suppose the stipulation "Do you undertake to give ten aurei in the first Kalends of March?" The money cannot be claimed on the day stipulated because the whole of that day must be allowed the debtor for payment at his discretion.'

easily lay too much stress on that fact, however. The mercantile world has always been a law to itself, and has usually found means of enforcing the observance of its established customs without the assistance of the State. Promissory notes were for centuries negotiable in England before the statute of Anne that made them so formally. On the other hand, we know that in modern times United States paper, at the period of the Civil War, could not circulate in California in spite of the Federal law that made it current.

As regards Greece again, readers of Becker's *Charicles* will remember how the young Athenian, on arriving at home after his sojourn in Syracuse, cashed his letter of credit at the bench of one of the trapesites, a class who corresponded to the Argentarii in Rome. The imaginary incident is founded on the case mentioned by Isocrates in one of his orations, in which a certain Stratocles, about to sail from Athens to the Pontus, by making the payment down of a sum of money in Athens, was able to draw the same amount on his arrival in Pontus. The plots in more than one of Plautus's plays, which probably represent Attic conditions at the period of the New Comedy, turn on the fact of a payment being made by a letter of credit, or something of the sort, at the critical moment. The Greeks in the Roman period had long passed the stage at which commercial transactions were hampered by any theoretical difficulty about the transfer of property by document. The Chirograph and the Syngraphe, forms of documentary transfers of money closely analogous to our own, had to be recognised by the Roman law. 'I rule the land,' said Augustus, 'but the law rules the sea.' The Rhodian mercantile code had become practically the law of the empire.

The Principle of Documentary Money.—If A has a payment of £100 in gold to make at a certain date, and if he obtains from B a written promise to furnish him with the funds by that date; if, moreover, B is well and widely known to be a man easily able, at any moment, to perform his promise, an unexpected result may ensue. The £100 in gold may not

be wanted at all; C, to whom A's payment was to be made, is very likely to say to A, 'If you will transfer to me your right to receive the £100 from B, I will release you from your obligation to deliver the coin.' C can do this the more readily probably, because he knows that D, in his turn, will gladly accept from him B's written promise instead of the actual money. D again can do the same, because he knows that E will be similarly inclined, and so on, all through the alphabet, and backwards and forwards as often as we please. There seems to be no obvious limit to the number of transactions which the £100 in gold, which lies in B's vaults all the time, can thus vicariously settle. The written promise may be not only a perfect substitute for the metal as far as each payment is concerned, but a preferable substitute. There would be considerable risk in the removal of the actual £100 from place to place, whereas there is little or none in the transfer of the documentary promise. The possibility that we thus discover of the settlement of thousands of transactions of £100 apiece by written promises that involve only the existence of one mass of metal of that amount, is surely calculated to dispel the crude notion of a definite and calculable relation as existing in any country, or in the world generally, between the quantity of gold available for the purposes of exchange and the level of prices. What I have described, however, is more than a possibility. We see that something very like it, something certainly not less wonderful, is realised under our eyes at this moment in England, when we find at any given date, that we have on one side of the account nearly £1,000,000,000 of demand liabilities, and on the other, twenty to thirty millions in all devoted to the purpose of meeting them; and when we find, nevertheless, that they are met without fail, from day to day, and from year to year.

Bearing of Extended Money on Prices.—We are familiar with the bimetallist argument, suggested in advance by Jevons, that if we regard gold and silver as two reservoirs, each subject to their own fluctuations, due to the separate influence of supply and demand on each, we should find

that by opening a connecting pipe between them, that is to say, by fixing a ratio between the metals, the fluctuations in both would be reduced, as the effects of any excessive supply or demand would be distributed over both reservoirs. The truth is, however, that nature, if we leave her alone, will open connecting pipes not only with the adjoining cistern called silver, but also with that called copper, with that called wheat, with that called iron; indeed, with every commodity that has a definite value expressible in figures. All are brought together into the almost boundless reservoir called 'money,' by the machinery of Bills of Exchange.

What is it then that moves prices upwards or downwards in the world? Variations in the quantity of money, you say, perhaps. But is there any conceivable ground for asserting that variations in the quantity of this substitute money are less effective in altering prices than variations in the quantity of actual gold? Substitutes will compete in the market surely on equal terms with the thing for which they are capable of being substituted. An English manufacturer turns out, say, twenty thousand yards of calico shirtings worth, perhaps, 2d. a yard. He despatches them to his correspondent abroad, and at once draws a bill against them for £160, or thereabouts, which he forthwith proceeds to discount. The amount is placed to his credit, and becomes 'money' for him in every possible sense, and for every possible purpose. It increases his purchasing power exactly as much as the discovery in an old stocking of £160 in sovereigns would increase it. If his fancy leads him to spend the amount in the purchase of a horse, his competition for horses will tend to raise their price just as much as would the competition of a gold-digger who had unearthed a nugget weighing forty ounces, and had had it coined into standard money. The true source of the purchasing power is indeed the calico shirtings. If its quantity were doubled while its market value was maintained, the purchasing power of its owner would be doubled too, and the effectiveness of his competition in raising the price of anything in the market which he proposed to buy would be proportion-

ately altered. In endeavouring to interpret the causes of the fluctuation of prices, therefore, it is plain that we must not confine our view to fluctuations in the available amount of the one substance, gold. The truth is rather that, as in the sphere of physics, the movements of every particle of matter aid in determining the movements of every other particle, so, in the sphere of economics, the movements both in the price and in the quantity of every commodity, exert an influence, imperceptible for the most part, no doubt, but yet real, upon the price of every other commodity.

It seems paradoxical, but is thus nevertheless obviously true, that the one means by which we can make sure that actual gold shall not be wanted in commerce is to make it absolutely certain that it will be forthcoming whenever it is asked for. Produce a state of things in which the belief that it will be thus forthcoming is universal and unquestioned and no one will ask for it. Cause the least doubt to arise with regard to that contingency, and there will at once be a general scramble for it. So it comes about that legislative attempts to increase the volume of money, by enacting that instruments of credit shall be legally dischargeable by payments in something else than gold—in silver, for instance—instead of really increasing the volume of money, at once cause it to shrink portentously. This was seen very conspicuously in America in 1893, when the mere threat of such legislation caused a rush for gold that threw all business into confusion, and put back the progress of the country for years. Make gold payments certain, and you thereby at once add to the volume of money the whole mass of its documentary substitutes.

The Quantity Theory of Money.—The reciprocal theory of value referred to in our introductory chapter, and the quantity theory of money are the same thing under different aspects. Gold being, as is supposed, precisely on a par with other commodities as a measure of value, and a rise of one shilling a quarter in wheat, let us say, being thinkable, as the theorists hold, in terms of an equivalent fall in gold, the next step is to conclude that in the actual world an

increase in the quantity of gold must cause a fall in its value, and that this fall must somehow or other be interpretable as a rise in general prices. It seems in vain to point out to such reasoners that at the beginning of the nineteenth century about £2,000,000 worth of gold was being got out of the ground annually, and that to-day the annual product has reached nearly £100,000,000, while, at the same time, the prices of most of the necessaries of life are lower now than they were then. The quantity theorists are still prepared to maintain that the fact must be there somehow, no matter how it is disguised. It is worth while, therefore, to ask whether any theoretical answer can be given to a theoretical deduction that leads us to results so widely at variance with fact. The theoretical answer has already been, to some extent, suggested in the remarks cited in an earlier chapter, to the effect that the gold from the mines, under modern conditions, comes first through the banks into the hands of producers, and by assisting production tends to cheapen products rather than to make them dearer. The demand for raw material will, no doubt, be increased, and this will tend, in the first instance, to raise its price, but does even theory tend to the conclusion that it will raise it in the long-run ? On the contrary, we know that, among reproducible commodities, under modern conditions, the ultimate effect of increased demand is to bring down prices. From whatever point of view we regard the case, Gilbart's opinion that, in the ordinary course of business, an increase in money tends to lower prices,[1] presents a problem that assuredly the theorists have to reckon with.

Examination of Mill's Example.—There is a profound fallacy, too, in this idea of a general level of prices as something coherent and rigid, something that is capable of being moved upwards or downwards in the world all at once, and all together. The conception of such a thing as existing has, however, taken deep root, and is hard to eradicate. Mill's treatment of the subject is, in this point of view, very

[1] *History and Principles of Banking*, p. 106.

significant. 'We might suppose,' he says, 'with Hume, that some morning, every person in the nation should wake and find a gold coin in his pocket; this example, however, would involve an alteration of the proportions in the demand for different commodities; the luxuries of the poor would, in the first instance, be raised in price, in a much greater degree than other things. Let us rather suppose, therefore, that to every pound, shilling, or penny in the possession of any one another pound, shilling, or penny was suddenly added. There would be an increased money demand, and consequently an increased money value, or price for things of all sorts. This increased value would do no good to any one; would make no difference, except that of having to reckon pounds, shillings, and pence, in higher numbers.' [1]

The strange thing is that Mill, after showing himself alive to the fallacy in Hume's example, which indeed had already been well pointed out by Sir James Steuart,[2] should have gone on himself to adduce another example which in reality differs from Hume's in no salient characteristic whatever. Suppose that the community were one of those in the new world of the present day, where every one practically was in possession of as much plain food, of as much wheaten bread, say, as he could want, would the increased money cause a rise in the price of such bread? Why should it? If no one wanted any more of it, what can be more certain than that no one would give any of his freshly gained wealth in exchange for any of it. The result, indeed, instead of being a rise in bread, might easily, as Sir Robert Giffen has pointed out, in parallel circumstances, be a fall. The poorest class could then afford to spend more on meat, and consequently would spend less on bread. Why, moreover, should not a large part of the community put aside some of their new wealth to meet future contingencies? If they did so, however, the money would get

[1] *Principles of Political Economy*, People's edition, p. 299.

[2] *Principles of Political Economy*, vol. ii. p. 103. 'Increase the money,' he says, 'nothing can be concluded as to prices, because it is not certain that people will increase their expenses in proportion to their wealth.' Hume and Mill, on the contrary, assume that every added shilling will at once be spent.

into the banks, and, like the gold from the mines now, would stimulate production, and in the end lower the price of products. There is no reason that I know of for supposing that an increase of coined money in people's possession would operate in any different manner on prices from that in which the general increase of wealth operates. The general increase of wealth appears to tend to reduce the value in the long-run, of a great many at any rate, of the articles of common use. What it raises are eligible residential sites, deer forests, Corots, Botticellis, old furniture, old china, and all the innumerable things for the possession of which the owners of surplus wealth compete with each other. The general level of prices conceived of as moving simultaneously upwards or downwards is a myth of the economists, and corresponds to nothing in the real world.

Index Numbers.—The height of the level is supposed to be indicated by index numbers, but index numbers refer to *res fungibiles* only, which makes up about one-fifteenth of the wealth of the country at any given moment. To treat them as synonymous with everything that is exchangeable for money is a sheer absurdity. In practice it would lead to results that are incredibly preposterous. By the application of index numbers, Professor Pigou tells us that 'a competent authority might be able in times of depressed prices to bring into the field of taxation real increments of value which appeared as decrements.'[1] That is to say that, although the value of a man's property has fallen, in the ordinary sense of the words, from £10,000 to £5000, he might still, as the result of the manipulation of index numbers, be actually brought in as liable for increment duty.

It is with much satisfaction that I find that this view, for the validity of which I have elsewhere contended,[2] as to the absurdity of treating the fluctuations in index numbers as indicating and measuring fluctuations in the value of gold, is in accord with the reasoned conclusions of the

[1] *The Policy of Land Taxation*, p. 24.

[2] See *Evolution of Modern Money*, p. 303.

eminent French statesman and economist, M. Yves Guyot. Index numbers, as he justly says, 'never can refer to everything that can be bought and sold,'[1] 'they take no account of fixed capital, land, houses, factories, shops,' and so on.[2] As to the fluctuations that they indicate, 'It is not,' he remarks, 'the value of gold that varies.'[3] After showing how the theory breaks down in practice, gold production being often on the rise while the prices shown by index numbers are on the downward grade, and *vice versâ*, he observes, 'These facts prove the mistake which Mr. Bowley, along with so many others, has made in thinking that index numbers could measure the value of gold.' M. Guyot, indeed, frankly regards it as impossible to measure values at all, 'unless they can be compared with an invariable type.'[4] His reasoning on the subject, moreover, has been found convincing by so able and so cautious an English economist as Mr. Harold Cox.[5]

Cairnes on Gold and Prices.—Cairnes is the only economist, so far as I am aware, who makes any attempt at an exposition of the manner in which an increase in gold production can raise the prices of commodities. It is briefly this: that the great profits now and then derived from gold mining, such as those that were realised in California and Australia in the late forties and early fifties, can draw away labour and capital from the production of other commodities, and can thus make these commodities scarcer and eventually dearer. M. Yves Guyot points out that the same thing precisely may happen in the case of great discoveries of coal or iron. Labour and capital may then also be attracted by them, and thus withdrawn from other industries, and the products of these industries may consequently rise.[6] It is further worth while to note that, under Cairnes' theory, the rise that takes place is due, not so much to the gold above ground as to the prospect of getting more gold out

[1] *La Science Economique*, ed. 3me, p. 202.
[2] *Ibid.*, p. 212. [3] *Ibid.*, p. 202. [4] *Ibid.*, p. 221.
[5] See *Spectator*, 26th October 1907.
[6] The same criticism on Cairnes' reasoning was made by myself independently in a former work (*Evolution of Modern Money*, pp. 307-308).

of the ground. The two things are by no means necessarily coincident. There may be, as there was at the start of the Californian diggings' period, a relatively small output, but immensely attractive prospects; or there may be, as there is at the present moment, an immense output, but—the industry having settled into its groove—no special attractions for new labour or new capital. The quantity theory traces the rise in prices to the gold above ground, the gold that actually enters the circulation, and thus Cairnes' theory, which relies mainly on the prospects, affords no support to it.

The Test of a Fall in Gold.—In the case of iron, no one would dream of identifying the rise in other commodities which the rush into the iron industry might bring about with a fall in iron. In the case of gold, on the contrary, this is held to be the only legitimate way of viewing the facts. But is it so really? A true and unmistakable fall in the value of iron we can, of course, easily identify as such. It is a diminution in the power of a given weight of it to purchase for us as much of the monetary substance as formerly. When we try to apply the same test to the gold, we are, of course, faced by the difficulty that the power of gold to procure gold cannot alter. We say, therefore, to ourselves that we must find some other test of the true fall in gold, and we rashly, as it seems to me, conclude that it must have fallen when we find that it has less power than it had before to purchase anything whatever that we choose to fix upon; thus putting any chance commodity in the place of the monetary substance, as a measure of value. We do not, of course, do the same with iron, or with anything else. We do not say that iron has fallen if, copper having risen, we can barter a ton of iron for less copper than formerly. The question, perhaps, then arises for some minds: Can there be such a thing as a true fall in gold? It is impossible, however, to really doubt for a moment that there can. If a process were discovered to-morrow by which—as was rumoured a few years ago—gold could be extracted *ad libitum* from sea water by any

one who chose to extract it, at a cost markedly below £3, 17s. 10½d. per ounce, the fall would be with us at once. How then would it manifest itself? Beyond all question, by the setting in of *distrust* of gold as a medium for the storage of purchasing power. Gold would then be no longer the most liquid of all conceivable assets. We should no longer think of values as being 'realised' as soon as they were made convertible into gold. Even with paper issues, it is only when distrust sets in that they begin to lose their value. The assignats, in spite of the activity of the printing press, maintained their value at par during the first nine months of their existence.

The Operation of Distrust.—Once the distrust of gold began to set in, however, even in the most indistinct and hesitating fashion, every one would soon begin to be afraid to accept gold in return for other produce, lest, as more of the metal was produced, the distrust should deepen yet further. If, however, every one began to be anxious to get rid of gold, no doubt prices would mount with a vengeance. An able economist in the last century, Fullarton, was much exercised as to the danger involved in the clause in the Act of 1844, which made it obligatory on the Bank of England to buy all the gold that was offered to it at £3, 17s. 9d. per ounce. If the distrust of gold were really a matter of possible practical concern, such a clause would, no doubt, be a serious danger. Possibly one of the first things that, in such circumstances, would happen would be the refusal on the part of the great governments of the world to coin gold in unlimited quantities for every one who brought it to the mints, together with the refusal to treat uncoined bullion as money, and we might see attempts made to limit the issues of gold by international agreement as the Latin Union now limits the issues of silver. It is idle, of course, to speculate on such contingencies. One may only allude to them to emphasise the distinction between a real fall in gold and the fancied fall which some of our economists are beginning to speak of as if it were already upon us. It is about as real as the 'appreciation'

that some of the same writers were so full of a dozen years ago. They argue that because there is an increase of supply there must be a fall in value; but if the fall is manifestly not there, there is no use in telling us that it ought to be there. The estimation of gold is a psychological fact that is open to the direct observation of any one.

Those who argue that gold must have fallen because the supply has increased, do not consider that there are many things, diamonds for instance, of which the supply may be, for a considerable period at any rate, largely increased without any fall in their value taking place, simply because the demand for them has increased *pari passu* with the supply. The peculiarity of the monetary substance is that in its case this operation of increased supply in causing a concomitant increase of demand is far more general and permanent than in the case of anything else.

Credit and Prices.—I have endeavoured, in the last chapter, to show how gold, in the first instance, attained the monetary position. Once it has attained it, and has, moreover, become also the nucleus of the credit system, other factors come into play to make the stability of its value yet more impregnable. There has been a good deal of controversy over the question, whether or not credit affects prices as money does. It would, it seems to me, be more to the point to inquire whether anything else but credit has any practical effect on prices that is worth mentioning. I have referred above to Bagehot's view as to the fixation of prices in the wholesale trade. He remarks, 'Prices in general are mostly determined by wholesale transactions. The retail dealer adds a percentage to the wholesale prices, not, of course, always the same percentage, but still mostly the same. Given the wholesale prices of most articles, you can commonly tell their retail price. Now, wholesale transactions are commonly not cash transactions, but bill transactions.'[1] This is as much as to say that prices in practice are determined by credit and by credit only, and that the sole way in which gold can effect

[1] *Lombard Street*, p. 140.

them, except in isolated and unimportant instances, is through its effect on credit.[1] Professor Marshall, similarly, in his evidence before the Gold and Silver Commission of 1888, had, as we saw, to concede that variations in the amount of the gold available could only get at prices to affect them through their effect on the rate of discount; that is to say, again, that it is credit which determines prices, and gold only affects them through its effect on credit. It follows, of course, from this, that the whole amount of gold in circulation as retail cash may practically be eliminated and left out of account when we reckon up the factors which determine prices. More of gold, as in Tooke's view,[2] more of convertible notes, is drawn into circulation when prices rise, and less again when they fall, but variations in the amount in circulation stand in the relation of effect, and not of cause to variations in the average market prices of commodities. This, too, is the view to which such eminent living economists as M. Yves Guyot in France, and President Hadley in America, appear to lean.

Granted, however, that variations in the quantity of gold affect the rate of discount, and that the rate of discount again affects prices, we are still face to face with a question to which it is extraordinarily difficult to give any definite answer, the question namely, how does it affect them. The effect of cheap money on some commodities is different from its effect on others. The immediate effects, too, are, in most cases, widely different from the ultimate effects. As argued above, as regards the means of subsistence, and as regards reproducible commodities generally, the tendency of an increased gold supply, and a consequently cheapened supply of loan money is to make them more abundant and cheaper in the long-run.

In conclusion, it is worth while to notice the inadequacy of one of the lines of abstract reasoning much relied on

[1] Sir James Steuart indeed had said pretty much the same thing already (*Works*, vol. ii. p. 372).

[2] There is evidence indeed that Tooke extended this view to the case of all real money (*Inquiry into the Currency Principle*, p. 62).

in regard to the question at issue. Walker, for instance, remarks that when we observe a fall in any commodity, say in wheat, we may set that fall down, straight away, as *pro tanto* a rise in gold.[1] From that proposition he and other bimetallists pass on to the entirely different one that a rise in gold—evidenced by its relative scarcity as shown by statistics—*causes* a fall in other commodities. The first proposition, however, applies, of course, just as much to cases in which it is definitely shown that the *cause* of the fall in the commodity in question is simply the reduction in the cost of its production or transport as to any others. If we suppose that wheat is now 8s. per quarter cheaper at Liverpool than it was thirty years ago, merely because it costs 8s. per quarter less to bring it across the Atlantic, that fall in its price would still come under Walker's rule that it may be called, if we please, a rise in gold. His proposition, thus, has plainly no bearing on causality at all, and has no sort of connection with the proposition that variations in the gold product necessarily affect market prices.[2]

[1] *International Bimetallism*, p. 254.

[2] Cf. Yves Guyot, *loc. cit.*, pp. 202-320.

CHAPTER XIII

THE CREDIT SYSTEM: SOME OF ITS PROBLEMS

Credit and the Creation of Capital.—Is the creation of credit ever the creation of capital? On the one hand, there are beyond question many commercial phenomena that appear, at any rate at first sight, to warrant the assertion that it is. On the other, we have in the background of our minds a well-founded suspicion of any reasoning, however seemingly cogent, that appears to point towards the conclusion that it is possible to create real wealth by a few strokes of the pen.

The classical instance of a phenomenon that seems to warrant the affirmative view is the Scotch 'cash credit' system. In Scotland, as we know, several of the banks, during some generations, issued notes to the amount of five or six times the bullion that was held against them, and did it with perfect commercial safety. The 'cash credits' based on these issues are said to have altered the whole face of the country. 'Enormous tracts of barren land,' M'Leod tells us, 'were changed into fertile cornfields.' It is hardly surprising that, in view of such a fact as this, he should have felt himself justified in asserting that these notes were a 'pure *addition* to the previously existing money,' were indeed a literal creation of capital. M'Leod, though a striking and vigorous writer, was, no doubt, an erratic one, and he lays himself open to obvious criticism at innumerable points. His German critic, Knies, a learned and patient investigator, has no difficulty in pulling to pieces many of his assertions. His assertion, for instance, that the cancelling of a credit, that is to say, the payment of a debt, may be equivalent to the destruction of so much property, is very justly exposed and refuted. When,

however, Knies has proved, in twenty or more closely printed pages, that a given sum of money cannot possibly be the property of two people at the same time, as M'Leod asserts, or comes near to asserting that it can, how much further ahead are we ? Such a fact as the Scotch fiduciary issue referred to, still remains a fact in the world's history, and one which, of course, has hundreds of parallels ; and Knies's theory makes no pretence even of giving any account of it. Mill's position in regard to the matter is an intermediate one. He comes consequently under the lash, both of Knies and of M'Leod. It is characteristic at once of his candour, and of his inadequate appreciation of the necessity of thinking out the questions on which he pronounces judgment, that we find him saying with emphasis on one page, that credit is nothing but 'a transfer of capital from hand to hand,'[1] and telling us on the next, that it 'creates purchasing power,'[2] that it affects prices just as money does, and that it may very completely 'supersede money.' It surely needs some explaining to make it clear to us how it can be that a fact or phenomenon which is a mere transfer of capital can come to be endowed with such wonderful causality in the affairs of life.

Two Kinds of Credit.—In approaching the investigation of the question, the first thing that strikes us is that credit is plainly divisible into two well-marked species. In the one we have such a fact as the simple permission to defer payments which a shopkeeper accords to his customers, or the advance which he himself obtains from a bank ; on the other, the acceptance by any of us of a bank-note as compensation for his goods or services. The first kind of credit is conscious, the second, for the most part, unconscious. No one, practically, when he takes a bank-note, recognises that, by taking it, he is lending money. In the first form again, we have very generally loans made by the wealthy to the less wealthy, primarily at any rate, for the convenience of the latter; in the second form, more often, loans made by the relatively poor to the relatively rich, and

[1] Book III. chap. xi. sec. 2. [2] *Ibid.*, sec. 3.

primarily for their own convenience. The connotation of the verb 'to lend' is, indeed, so completely bound up with lending of the first description that we seldom apply it naturally to lending of the second sort. The latter sort of loans, when made to a bank, we call 'deposits,' and it takes an effort of thought to realise that deposits are loans at all. It was evidently the first sort of credit that was generally before the mind of Knies, the second that was before the mind of M'Leod. The first is a simple and straightforward matter which presents no puzzles or contradictions. The second, on the contrary, is full of paradoxes, and of as yet unsolved, or only half-solved, problems.

Where, indeed, outside the sphere of credit, do we find anything analogous to such a fact as this, that gold, or what is looked on as its perfect equivalent, may at one moment be demanded with urgent insistence by a whole community, and yet next moment, when it is brought within reach of every one who has a right to it, it may turn out that practically no one cares to take possession of any of it. All, on the contrary, are now perfectly satisfied with the simple fact that it is at length well within their reach. As a writer in an old number of the *Quarterly Review* [1] puts it, 'The power of procuring money is tantamount to the actual possession. To use a scholastic phrase, money *in posse* is equivalent for all purposes to money *in esse*.' What else in the world is there *in posse* that is in any way equivalent to the same thing *in esse*? An eye-witness of the panic of 1847 says, 'No sooner was it known that notes might be had, than the want of them ceased.' In the course of ten minutes the panic vanished like a dream.

As we proceed again with our investigation, further problems present themselves. We are told, and, on the whole, rightly told, that 'banking consists in buying debts with promises to pay,' [2] and that 'A banker is a trader whose business consists in buying money and debts by creating other debts.' [3] The puzzled outsider, however,

[1] July 1822.

[2] H. D. M'Leod, *Theory and Practice of Banking*, 3rd ed., vol. i. p. 278.

[3] *Ibid.*, p. 275.

may ask, 'What is at the bottom of it all? why do people want to substitute one debt for another, or why do they give their money to a banker in exchange for nothing but a right of action against him; and how is it that the banker can make a profit by permitting himself to be substituted as a debtor for somebody else?' The answer to these questions is to be found in connection with an aspect of credit to which it will be worth while to devote some attention now.

The Importance of Conspicuousness in Banking Credit.—We may call the first of our two sorts of credit, for the sake of distinctness, 'simple credit,' the second 'coinable,' or 'banking credit.' We have seen that in regard to the last, it is usually the relatively poor who lend to the relatively rich. It may be helpful to endeavour to find an answer to the question, why is it that they do so. To put the underlying conditions of the problem in the simplest form possible, let us revert to our illustration used in a previous chapter, that of the three individuals, A, B, and C, among whom A holds B's written promise to furnish him with £1, £5, or £100, in gold, whenever he is called upon to do so, and let us suppose that C is asked to release A from his obligation to pay, say, the £100 in gold, if B's written promise is handed over to him instead. Now, it is obvious that a necessary condition to the possibility of C's willingness to release A from the original obligation would be the fact that he was perfectly satisfied in his own mind as to B's readiness and ability at any moment to perform his promise. That, however, alone might not be altogether enough. It is evident, at any rate, that C's readiness to accept the promise instead of the gold would be greatly enhanced if he were not only satisfied himself as to B's honesty and the adequacy of his resources, but if he had, at the same time, good reason to believe that D, E, F, and the rest were also satisfied on the same points, and that any of them consequently to whom he might happen to have occasion to make a payment would, in their turn, quite gladly take from him again the promise instead of the gold. As gold itself originally

became money in virtue of its 'acceptability,' so the credit document becomes converted into the equivalent of money in virtue of the very same characteristic.

We see thus that, whereas in the case of simple credit, all that is of importance for the creditor to consider is the solvency of his debtor, in the case of banking credit another consideration altogether becomes relevant, that of his conspicuousness, his conspicuousness, that is to say, in respect of the one attribute of solvency. Let us suppose that B is a great banker, a Fugger or a Rothschild, perhaps, whose firm has been notoriously wealthy for generations past, his promise will be readily taken by any one as the perfect equivalent of cash. It is evident further that, given the promise to pay of any solvent individual who, however, is lacking in the conspicuousness necessary to convert his promises into cash, if the great man can be induced, for a consideration, to exchange recorded promises with the small man, the small man's promises, too, can be brought up to the level of acceptability of the great man's, and can thus be made to function as money. Exchange entered into for the purpose of thus levelling up the less conspicuous promises with the more conspicuous forms the ultimate meaning of many transactions that are not otherwise explicable.

Knies's Formula.—Knies thinks that he has found a formula that should solve every problem in credit when he defines it as the exchange of present services for future services, or, as we may put it, of money down for money in prospect, but, though the Time element, no doubt, explains a great deal in banking, it cannot anyhow be made to explain everything. The most obvious illustration of the formula, 'money down for money in prospect,' is the discounting of a three months' bill. Even this illustration, however, is only perfectly applicable when the discounter means to hold the bill till its maturity. Most of the bills that reach the London money market are discounted by people who have no such intention. The bill brokers and discount houses ordinarily pass them on to the banks immedi-

ately that they come into their possession. They give £99, say, for that which will, no doubt, have a value of £100 in three months' time, but which, at the same time, has to them a value of something over £99 at the present moment, otherwise they would not buy it. It is for the sake of this 'something over,' indeed, that they do buy it. What we see in such a case is clearly the levelling up of the less conspicuous with the more conspicuous credit.

Cases that the Time Element does not Explain.—To take another example : when we see vast sums set down as bank deposits, it is, of course, a mistake to imagine that they represent so much accumulated wealth. What happens is, to a great extent, this : the bank makes an advance to its customer, and the advance appears as a deposit. The deposits on the liability side of a bank's balance-sheet thus ordinarily increase *pari passu* with the loans on the assets side.[1] Where, then, does the Time element enter in connection with such transactions as these ? The banker, in such cases, simply takes an immediate right of action against his customer, which is not available for use as cash, and gives him an immediate right of action against himself which is. Or, turn again to such a transaction as this : the deposit with the Bank of England by one of the Joint Stock Banks of the sum which it means to hold as a part, perhaps practically as the whole, of its cash reserve. It gives cash, or probably value, in the shape of securities down, and it gets what it reckons as cash down also. It gets an immediate right of action against the Bank of England, and this it is able to treat as cash *par excellence*, cash good enough to form the basis of all the credit that it creates. Its own promise to pay is cash good enough for most purposes, but not quite good enough for all. It therefore procures the Bank of England's promise, which all the world accepts as absolutely equal to gold itself. The Time element evidently does not enter into transactions of the type of the two last mentioned at all. The whole explanation of them is to be found in the levelling up of the

[1] Hartley Withers, *The Meaning of Money*, p. 64, *et seq.*

less conspicuous with the more conspicuous credit. In essence what happens in such cases is not very different from that which is effected when a rich man fortifies the credit of a poorer man by becoming surety for him. The interesting difference, however, is that in banking this fortifying is done by way of an exchange of recorded promises; and we find in this fortifying of the lesser credit and its elevation to the level of the greater, the additive element that warrants, or seems to warrant, the assertion that the creation of credit is the actual creation of capital.

Credit Creation not Arbitrary.—Are we then finding ourselves led in the direction of the conclusion that capital can be created by a stroke of the pen? Two replies to this query suggest themselves. In the first place, it manifestly is not open to any one who pleases to create cash out of credit. If you or I, for example, were to attempt to issue our promises to pay with the hope of keeping them in circulation, the chances are much more than a thousand to one that no one would accept them. If we go back to the time when it was open, as far as the law was concerned, to any one who pleased to issue such promises, we find that those houses that were best endowed with the attributes calculated to enable them to survive in the struggle for existence are those that have survived. Among these attributes, the possession of considerable capital to begin with, together with the willingness to risk it in such a business, has, no doubt, counted for much. Add to this judgment, foresight, hard work, and allow something for luck, for the privileged opportunity, and we have all the conditions of survival present, the conditions which in the case of certain firms have made the creation of the sort of credit that is convertible into cash a possibility. But then these are just the conditions which would have made the creation of wealth in any other branch of trade or production possible. The establishment of a position of sufficiently conspicuous solvency to enable a man, a firm, or a company to convert their promises into cash is clearly analogous to the creation of 'goodwill' in a business of any other sort. Any one of

us indeed can now participate in the profits to be derived from the conversion of credit into cash by purchasing shares in a joint stock bank, or in a Scotch bank of issue, but then, of course, we would have to pay for the privilege just as we would for the privilege of sharing in the gains of any other profit-making business. The creation of credit convertible into cash thus appears to have a cost of production, and one that will be found to be, in the long-run, about equal to the cost of production of wealth by any other means.

Qualification of M'Leod's View.—In the second place, it may be said that if M'Leod had confined himself to the assertion that the creation of credit may be equivalent to the creation of cash at a given moment, his assertion could not have been gainsaid. Any one of us who uses a fiduciary note for the same purpose as that for which he would have used a sovereign, is witness to such a conversion. To call this credit-cash 'capital,' however, is, no doubt, to accord to it in prospect too much of a necessary validity. It may, indeed, turn out in future to possess such validity, but, on the other hand, it may not. We know unhappily that the cash that is created by credit may partake of the nature of a mirage. Securities begin perhaps to rise in value, and as they rise, may be used as increased collateral for fresh loans. These loans again may send up yet further the prices of the same and other securities, and this fresh rise, in its turn, may appear to warrant yet further lending. The process appears to have no obvious limit. The new purchasing power has all the appearance of cash for the time being, and indeed is cash for those who get out at the right moment. The time, however, comes at length when people begin to doubt whether values are as sound and as well founded as they should be, and then the credit-cash vanishes and leaves not a rack behind.

We seem thus, in inquiring to what extent the creation of credit cash may be taken as equivalent to the creation of capital, to be driven back upon the more elementary inquiry whether such cash has been created in conformity

with the general conditions of safety in banking, and we are thus again yet further driven to ask, what are those conditions? As regards the large proportion of banking transactions that consist of the discounting of bills drawn against commodities that are passing from hand to hand, we can see without difficulty that what sound credit really imports is the economy of cash in the transfer of existing goods. Goods of a certain value in money are in the end set off against goods of an equal value, without the mediation of actual cash. The documents that we, in such a case, call credit documents, and which we can create with a stroke of the pen are obviously mere intermediaries. They have behind them the value of the commodities, the sale of which has given rise to them. As regards them, the banking system seems to be literally a system of organised barter. When, moreover, we pass on to the consideration of other banking transactions, we have, I think, still to keep this same general view of their nature before our minds, and to inquire to what extent they can be made to fall under the same category. It has been contended indeed that no banking is sound that is not reducible to the simple transfer of goods.[1] This, however, is to put too unreservedly a view that yet contains a certain element of truth.

This much, at any rate, is certain, that in all cases the one thing which a banker has to consider when asked to grant a right of action against himself, which can be used as cash in exchange for a right of action against a private borrower which cannot, is the nature of the security offered. He must consider what, perhaps, the borrower is prepared to pledge in the shape of collateral, or, more generally, how his personal security can be estimated. Personal security, no doubt, takes account of other things besides actual possessions, but the main consideration in connection with it is, for all that, the amount of the man's total wealth of every sort. This fact again points to the further conclusion that the real meaning of banking, with the apparent creation of capital that it involves, is the bringing of the more or

[1] Cf. Professor Laughlin. Decennial publications issued by the University of Chicago, vol. iv. p. 7.

less undefined wealth of the world into the field of immediately available purchasing power.

Gold, it is frequently said, is the basis of credit, but when we compare our relatively minute reserve of gold in the Bank of England with the portentous amount of the liabilities against which it is held, we seem to be straining metaphor unduly if we call the first the basis of the second. Sir William Petty remarks acutely that 'the precious metals are wealth always'; other things are 'wealth here and now.' To find the true basis of credit, we must, I think, add 'the wealth here and now' to 'the wealth always.' Some considerations, however, with regard to the nature of wealth itself that are not immediately obvious, seem here to be relevant.

The Anticipatory Element in Wealth.—Cernuschi appears, no doubt, effectively to annihilate the possibility of the creation of credit that can be equivalent to the creation of capital when he puts his reasoning in this shape: 'The balance-sheet of every individual contains three accounts, existing goods, credits, and debts. But if we collected into one the balance-sheets of every one in the world, the debts and credits mutually neutralise each other, and there remains nothing but a single account, existing goods.' There is, however, one flaw in his argument, that is the identification of all wealth with 'existing goods.' Capital has been appropriately enough defined as being in modern business usage 'capitalised presumptive earning capacity.'[1] It is, at any rate, impossible to escape from the conclusion that goods that do not at present exist, but that have yet to be produced, necessarily enter largely into our conception of wealth. Take the case of a new gold mine for example. You have several shafts sunk at various points along the reef, and connected by drives, and have numerous assays made. You get the report of an authoritative expert who predicts, with some confidence, success for your mining operations. The mine becomes at once a saleable commodity, and becomes perhaps adequate security for a loan

[1] Veblen, *Theory of Business Enterprise*, p. 127.

of large amount, although the material wealth which the property in it guarantees to its owners, exists as yet only in anticipation, is something that as yet, at any rate, has to be won from Nature, and which quite possibly may never be won at all. Through the banking and credit system, wealth of every sort can be converted into immediate purchasing power, and the case of this wealth, which consists in the anticipation of goods yet to be produced, is no exception to the rule. Such wealth, indeed, is in practice coined every day into the cash that is needed to carry on the industry that produces the goods in which its ultimate realisation or validisation consists.

It is when this anticipatory wealth is converted into cash that phenomena present themselves, which seem most strongly to identify the creation of credit with the creation of actual capital. The Scotch cash-credit system, already alluded to, forms one instance in point. Another that is in some respects even more interesting, is to be found among the recent developments of agricultural credit on the Continent. The Raiffeisen Societies consist of groups of, generally speaking, extremely poor peasants. Very few of them singly could borrow anything on their personal security from any bank. The richest among them probably could not borrow more than a trifle. The fact, however, of their forming themselves into a society, becoming liable jointly and severally for the repayment of all the loans made to the corporate body, and appointing committees of administration and supervision, puts the matter in an altogether different light. A security is at once created the validity of which is now very generally recognised by the other lending institutions of Germany. When again several of the societies co-operate to form a Central Bank, the conspicuousness of their credit is, by this means, greatly enhanced, and the security that they can now offer becomes a readily marketable one. Many millions, as we know, have been lent to these societies, and the losses incurred have been so small as to be negligible. The remarkable discovery, indeed, has been made that the groups of poor peasants thus organised are the most certain

of all repayers of borrowed capital, and the natural result has followed that the rates of interest at which they can obtain money, lent to them on purely business principles, have become quite reasonable. The system has been described as the 'capitalisation of honesty.' Honesty is one of the factors capitalised no doubt. There is also, however, to be taken into account the increased probability that the borrowed money will be wisely expended owing to the collective brains and experience of the society being brought to bear on the use to be made of each several loan that is granted. The Committee must always know for what purpose the money asked for is to be used. The famous economist, Leon Say, was much interested in the system. He saw, it is said, in this conversion of personal security into marketable collateral for loans on a great scale credit in its most advanced form.

A good deal of controversy has been expended on the question whether the efficiency of the labourer and the ability of the captain of industry can justly be described as actual wealth in being or not. Not a few economists hold that they can. It seems, however, much more in conformity with common sense and common usage to describe them, not as wealth itself, but as the causes of wealth. We are now, however, led to the conclusion that they have, at any rate, this much in common with actually existing wealth that they can, through the operation of the credit system, be converted, like it, into immediately available purchasing power, and that this is the case even when these causes are causes of a psychological character.

Summary of Chapter

To recapitulate briefly the steps of our reasoning : credit, if it cannot justly be said to be convertible into capital, is certainly, at any rate, convertible into cash at a given moment. The highest credit in this country, that of the Bank of England, is made into cash by its immediate and unconditional convertibility with gold, and other banking credit is similarly raised to its level, and can thus

also function as cash. All through the banking system, we see the same process at work, the raising of the less conspicuous credit to the level of the more conspicuous, by the exchange of rights of action, known on the one side as advances, and on the other as deposits. Whether this credit-cash thus created can, in a given case, be described as capital or not, is a question that no one can answer off-hand. Looking back at the past from our vantage ground in the present, we might say that the advances made under the Scotch cash-credit system were a real creation of capital ; but when this assertion is carefully looked into, what it really means is this and nothing more, that they were an anticipation, which Time has proved to have been a valid one, of the operation of causes that have been effective in producing wealth, and that on a great scale. We can see thus that the theory of credit is not a separate thing from the theory of value, but is merely indeed one aspect of it ; and we are led to this further conclusion, one, I think, of some importance and interest, that the most effective and the most indispensable of all the factors in the production of wealth is foresight.

CHAPTER XIV

CREDIT CONTINUED : SUBSIDIARY PROBLEMS

In the last chapter I endeavoured to grapple with some of the principal problems arising out of the development of credit. There are, however, of course, a great many subsidiary questions of much interest connected with it. In the present chapter I propose to take up the investigation of a few of the most important among the number.

Panics ; Their Alleged Periodicity.—The idea still lingers in the writings of some economists that there is something in the theory of a necessary ten yearly recurrence of panics ; and even in their suggested connection with the constitution of the solar system. The notion, however, rests exclusively on the occurrence of the three panics of 1847, 1857, and 1866. Nothing in commercial history, either before or since, gives any support to it. Forty-six years have now elapsed since the Overend Gurney crisis, and we have had nothing like it in the interval. Again : to go back to the earlier period ; in the thirties there were two crises of about equal importance, one in 1836, and the other in 1839, and during the yet earlier years of the century commercial catastrophes such as the modern world has had no experience of, befell the country at amazingly frequent intervals. In 1810, there was a crisis that led, we are told, to the destruction, or at least the suspension, from business of 'a great majority of the old establishments connected with the ports of the continent of Europe and the United States of America.'[1] A brief interval of prosperity followed, then 'a succession of hurricanes'[2] swept the country. Twenty-nine banks, Tooke tells us, fell in 1814, twenty-six

[1] Tooke, *High and Low Prices of Thirty Years*, p. 38. [2] *Ibid.*, p. 39.

in 1815, and thirty-seven in 1816.[1] The number of stoppages and compositions that occurred during the period, were said to have been equal to half the traders in the kingdom. It was, of course, the time of our great struggle with Napoleon, but the circumstances that led to the crisis of 1810 were, from the national point of view, all of them favourable ones. They were mainly good harvests at home and success abroad in rendering nugatory the French blockade, with the fall of prices and the collapse of speculation that ensued on these events.

Still earlier in our history men lost their heads, as we know, even far more completely. 'Landlords,' in the days of the South Sea Bubble, 'sold their ancestral estates, clergymen, philosophers, professors, dissenting ministers, poor widows, as well as the usual speculators on 'Change, flung all their possessions into the new stock.' [2] It was possible then to float companies with some success for the carrying out of projects the nature of which was 'yet to be disclosed.' The epidemic of error and miscalculation was then universal and world-wide. The illusion of reality and permanence in the inflated values was far more thorough-going than anything of which the nineteenth or twentieth centuries have any experience.

The Trend towards Stability of Value.—The trend towards greater stability in values indeed is among the most distinct of all the trends in the economic history of our epoch. Many of the causes that in old times rendered values unstable and incalculable are being, one by one, left behind by the modern world. Actual depreciations of the metallic currency are everywhere things of the past. Over issues of paper-money are coming to be confined to the most backward of South American republics. Even English economists have almost ceased to advocate the equivalent of currency depreciation in India. Inflations of credit, again, are, in this country at any rate, assuming a form in which they affect special markets and professional specu-

[1] Much larger numbers are mentioned by another writer; his definition of a bank was probably a different one from Tooke's.

[2] Lecky, *England in the Eighteenth Century*, i. p. 323.

lators only, and in which they concern less and less the public as a whole. When we recall the fact that in 1847 the Bank of England allowed half of its none too large stock of bullion to be withdrawn without raising its rate of discount above five per cent., we need hardly resort to the sun-spot theory to account for the crisis of that disastrous year. The discovery, indeed, of the possibility of controlling the outflow of bullion by raising the rate of discount, not to mention its control by other more recent devices, had not then been made. Every fresh lesson learned by the banking and commercial world tends in the direction of increased stability, and with it in the direction of making a given sum in gold support safely a greater and ever greater superstructure of credit.

The Central Bank Question.—A tendency, too, towards a more closely knit organisation of the whole body of banks under the control, more or less, of one central institution is one that seems to be making itself felt in every important commercial country. In theory the Bank of England is only one bank among many, and, twenty or thirty years ago, the representative men among its directors were in the habit of vigorously repudiating the suggestion that it had any special responsibility in connection with the maintenance of the nation's gold reserve, or the warding off of crises. Circumstances have been too strong for them, however. No one repudiates those responsibilities now. On the contrary, the memories of the crises of the past appear to have brought with them a vivid conviction of the necessity of being on the alert to check developments which may, even at some fairly distant future date, become critical. In 1906 a speculative movement in American stocks was checked by the intervention of the Bank of England, which discountenanced the advances by London Banks which had made it possible.[1] Had that movement not been checked in time, the United States crisis of the following year would undoubtedly have hit us much harder than it did. Increased supervision on the part of the bank is one of the manifest probabilities of the future.

[1] O. W. Sprague, *Economic Journal*, 1908, p. 356.

Bagehot's view, as we know, was that the many reserve system was in itself the best, though, as we had drifted into the one reserve system, it was impossible, he held, now to think of altering it. As regards his theoretical position, Professor Dunbar expresses dissent, and apparently with good reason. As a matter of fact, in America they have discovered, ever since 1860, that when a crisis is upon them, or is believed to be impending, the first necessity is to consolidate their many reserves practically into one.

The key to the situation lies in the very general recognition of 'The Expansive method,' as the only one which can be adopted with any reasonable prospect of success in the face of a panic. Let the banks attempt to store their cash in such circumstances, refusing to the mercantile community the accommodation that would be granted as a matter of course in ordinary times, and it becomes certain that a crisis will be precipitated. In Great Britain, in such a case, the Bank of England steps in and causes it to be felt universally that every security which would be looked on as a good security at any other period will be treated as a good security still.

In New York, in 1860, on the contrary, each bank on the approach of the crisis, naturally thought first of strengthening its own resources, and was inclined to let its neighbours take care of themselves. This, however, it was soon discovered, would necessarily mean disaster for all. Accordingly the organisation of the Clearing House was brought into play to meet the situation. 'The banks agreed that, for the purpose of enabling them to expand their loans, the specie reserves held by them should be treated as a common fund, and, if necessary, should be equalised among the banks by assessments laid upon the stronger for the benefit of the weaker, and that for the purpose of settling balances between the banks, a committee should be appointed with power to issue certificates of deposit to any bank placing with them adequate security in the shape of stocks, bonds, or bills receivable, and that these certificates should be received in payment by creditor banks. The effect of this arrangement was that any bank which experienced an unusual demand

for specie would be supported by the whole of the common stocks, and that the debt to the others which it thus incurred, could be met by a pledge of its securities. Whatever course might be taken then, any bank was as strong in specie as any other.' [1] The Clearing House, in fact, was converted into a central bank for the occasion. A similar method has been adopted on several occasions since, and commercial opinion in the United States seems now to be in favour of establishing under some name or other, a Central Bank permanently.

We may see, perhaps, in this metamorphosis of the Clearing House something analogous to the changes of function that often characterise the evolution of species in the lower world. The Clearing House took its origin in the eighteenth century from the meeting of the clerks at a tavern to set off their checks against each other, and thus to save themselves the trouble of visiting each other's banks. They would be amazed to learn what, in the end, has come of their simple device. The transformation of the swim bladder into the lung is hardly more remarkable than the development out of this device of a governing body called to take the helm in times of danger.

Perhaps, again, it may be said with some truth, that we have in the repeated recognition by the Bank of France of the necessity that exists, in its own interests, of coming to the relief of drains upon the Bank of England, the hint of a coming international organisation that may yet be of great significance in the world. The suggestion, at the same time, that there is in the tendencies which this development indicates anything that is already adequate to the maintenance of peace among the armed nations of Europe is surely among the idlest of conceivable fancies.

Banking Credit a Modern Phenomenon.—We dealt, in the last chapter, with credit under two headings—' simple credit ' and ' banking credit.' The phenomena of the latter appear to be distinctly and exclusively modern. M'Leod indeed represents Demosthenes as saying that there are

[1] Dunbar, *Theory and History of Banking*, pp. 81-82.

'two kinds of property, money and general credit,' and that 'our greatest property is credit.'[1] If the translation truly represented the original, we should, no doubt, be forced to look in the Athens of the fourth century B.C. for a very surprising anticipation of the commercial conditions of nineteenth-century England. What Demosthenes was thinking of, however, was apparently the value to the community of that confidence (πίστις) which makes it possible for the posssesor of spare capital to lend it to the man who wants it, and can use it. Of credit as a property, in M'Leod's sense, it is, no doubt, true that 'Demosthenes had never so much as dreamt.'[2]

What is distinctly modern is the fact of 'loans'—if we may call them such—made by lenders who, strange to say, have no intention of parting with the use of what they lend. 'In the ordinary case of lending,' to quote M'Leod, 'the lender deprives himself of the use of the capital he lends. But when a person pays in money to his bankers, it is not his intention to deprive himself of the use of it, on the contrary, he means to have as free a use of it as if it were in his own purse.' When this happens, we have the curious phenomenon presented of the same sum of money functioning apparently as the property of two people at once.

Such seems to be the case with the 'money at call,' for example, which is such a puzzle to the outsider who dips into the city article in his morning paper. What sort of people, he asks himself, can these be who borrow thousands upon thousands for one day only, and what sort of use can they make of it if they have to give it back the next day. It consists, of course, mainly of money which the banks lend to the bill brokers and discount houses. Though borrowed each day for the day only, these loans are to a great extent practically continuous at varying rates of interest. The money borrowed to-day will, for the most part, be borrowed again to-morrow, and also, for the most part, by the same people. The loans are thus, every shilling of them, used by the borrowers, but are they not used, at the same moment, by the lenders also? The bankers treat them as part of their

[1] *Loc. cit.*, vol. i. p. 131. [2] Knies, *loc. cit.*, vol. ii. p. 74.

reserve, as the cash that is the basis of the fresh credit that they create.

The Insurance Principle in Banking.—The appearance thus presented of the same sum of money as being used by two people at once, which, taken literally, is, of course, an impossibility, as Knies, Thornton, and others justly enough contend, becomes, perhaps, more comprehensible if we take account of the insurance principle in banking.

This principle presents itself most obviously in connection with a fiduciary note issue. Any one can understand how it is that a banker does not need to hold gold against every promise to pay that he launches on the world. If these promises are for small sums,[1] and if his credit is well-established, he may fairly reckon that, in the ordinary course of business, the retention in cash of about twenty per cent. of his total issues will suffice for meeting all the notes that will be presented for payment; the remaining eighty per cent., therefore, he can use otherwise for profit-making purposes, while the notes are, at the same time, also in use by the public.

Something similar again happens with regard to cheques, though the manner in which it happens is less obvious. Cheques practically do not circulate at all. The case is well put by Hadley. He takes the example of a manufacturer who brings a bill for $1000 to a bank, and gets it discounted. If the discount rate is six per cent., the bank deducts three months' interest at six per cent.—$15, and credits the manufacturer with $985. This he probably leaves on deposit with the banker. 'The bank is reasonably sure that the total amount of cheques drawn in a single day will form but a small fraction of its whole deposits. It therefore keeps but $200 of the $985 as reserve, and can use the balance as a means of discounting other bills.'[2] Here, again, you have the appearance presented of the same sum of money being used at the same time by the depositor and the banker; and if you concentrate your attention on

[1] Notes for large sums practically do not remain in circulation at all.

[2] *Economics*, p. 244.

any isolated case, you can hardly deny that such a thing might happen. When you look, however, at the general current of events, you see that it is practically only the money that the average depositor is not at the moment using that the banker can feel that he may safely dispose of.

The difference and, at the same time, the parallelism between the case of notes and the case of cheques, may be thus summarised. The cheque, like the note, is virtually, in normal circumstances, a banker's promise to pay the amount for which it is drawn. It is in the position of an accepted bill of exchange ; the possession of the depositor's funds by the banker standing legally in the place of formal acceptance. Suppose then that the manufacturer's bill, in the case cited by Hadley, had been paid for in notes, the banker would then indeed issue promises to pay up to the full amount less discount, but would reckon that, at any given moment, eighty per cent. of these promises to pay would remain in circulation. In the case, on the other hand, of the manufacturer being credited with the amount, and being allowed to draw cheques against it, though the banker would himself then issue no promises to pay, he would give his authority to the depositor to issue them on his account to the full amount of the bill, less discount. At the same time, however, in this latter case he could reckon that, taking the whole body of his depositors together, they would only issue these promises to pay to the amount of twenty per cent. of the total of deposits, and would thus leave the remaining eighty per cent. at his disposal.

That some twenty per cent. or so is enough to hold against a fiduciary note issue, or against a similar liability in deposits, is certainly a fact that no one could have foretold *a priori*. Experience alone has brought it home to us, and has done so, it must be said, in spite of a strong preconception against any such development. When the system first emerged in England, as it did in connection with the goldsmith's notes in the seventeenth century, it was looked upon as a dangerous abuse ; and this view of it was still the inspiring idea of the famous banking legislation of 1844 and 1845. The only effect, however, of these Acts, on credit generally,

has been to stimulate its creation by cheques instead of its creation by notes.

It is natural enough that the use of the note should precede the use of the cheque in the development of a credit system. M'Leod is right in insisting on the fact that, in the one-pound note, say, we have, in ordinary circumstances, a material object endowed with value precisely similar to the value of that other material object, the sovereign, however it has come to be so endowed. The ordinary man thus passes insensibly from the use of sovereigns to the use of notes. Presently, however, he realises that he is trusting the bank by accepting its notes, and feels that if he is trusting it in one way, he may as well trust it in another, and so leaves his money with it on deposit. Such a resort to credit transactions in either case Knies would endeavour to bring under the head of a sparing of metallic money; while M'Leod would bring it under the head of the creation of substitutes for such money. Of the two, M'Leod's view is surely the nearer the truth. We can hardly reasonably be said to spare our £20,000,000 or so of bank reserve to such an extent as to meet our £900,000,000 of demand liabilities.

The Bank Reserve Question.—Just as the issue of notes to several times the amount of the bullion held against them was, in the first instance, and indeed, in many quarters, was, up till quite recently, regarded as a dangerous abuse, so, on a first view at any rate, the whole system based, in this country, on the insurance principle, appears full of at any rate theoretical peril. Even when we recognise that a bank reserve of between twenty and thirty millions sterling is all the cash that we have to stand against demand liabilities of £900,000,000, the whole truth as to the magnitude of our total liabilities is not stated. For generations past we in this country, and we alone, have followed the straightforward policy of treating a bill—if, beyond question, a good one—for £100 or £1000 sterling as an indefeasible claim to its face value in gold, and our course of action has been vindicated by the fact that it has made London the

Clearing House of the world, and has brought us untold millions of profits in the shape of banking and commission business. We have to reflect, too, that in a time of crisis it has come, as we have seen, to be recognised that it is the special business of the Bank of England to see to it that the holder of no good banking security who applies for gold shall be sent away empty-handed.

The net result, however, of all this is the startling fact that every good banking security in the world, as well as every good security which any one is in a position to create, is a potential liability against the Bank of England's gold reserve. The bank has thus nowadays assumed a position in which it is responsible for the meeting of immense liabilities in the creation of which it has had no say whatever. Its so-called liability indeed appears to differ profoundly in its nature from anything that we ordinarily think of as the liability of any other banking or mercantile concern. It is not, like theirs, the result of risks undertaken in pursuit of profit, but is purely the creation of public policy.

Bagehot expresses the opinion frankly, in regard to his own day, that it is 'not possible to assign a superior limit to the demands which, by means of the banker's balances, may be made upon the Bank of England.' He thinks, too, that, at the time when the French Indemnity was being paid over, the German Government 'could have broken the Bank of England if it had liked.' It showed, of course, on the contrary, great consideration. If things have altered since Bagehot's day, it has been in the direction of increasing, not of lessening, the theoretical dangers of the situation. The adoption of the Gold Standard by so many countries has, Mr. Withers maintains, 'greatly intensified the responsibility of the Bank as the custodian of a gold reserve which is liable to be drawn on at any time from all quarters of the habitable globe from which a draft on London may be presented.' [1]

How, then, we may ask, does all this bear upon the question of the adequacy, or inadequacy of our present gold reserve. As a mere banking question, and as regards

[1] *Loc. cit.*, p. 210.

ordinary circumstances, it may fairly be argued that if it seems, on the one hand, to emphasise the greatness of the disparity between the reserve and the liabilities, on the other it points, quite as unmistakably to the impossibility of mending matters even by a course of action which should double or treble its amount; and we are thus thrown back for guidance on the general results of experience. We must then recognise that, after all, the reserve, for nearly half a century past, has shown itself adequate to the task of averting commercial disaster. It is, as Bagehot says, a 'safety fund,' and it certainly appears to have fairly well secured the safety which is the object of its existence. It is worth while to reflect also that we are not really so dependent, as we seem at first sight to be, on the reserve alone to meet our liabilities. In the past we have always had a second line of defence in the resources of the outside world. By raising the discount rate, we have always been able to reckon on drawing in money in apparently limitless quantities from abroad. In 1907 we sent £25,000,000 to America, without reducing the reserve which before the crisis stood at £24,000,000, below £17,000,000.

The question thus as to the amount of cash which it is necessary for the Bank to hold as a reserve, becomes evidently one on which it must be exceedingly difficult for any one to pass an unchallengeable opinion. No doubt it might be increased with advantage; at the same time it must be said that an idea seems often to run in the minds of those writers who treat its inadequacy as an obvious truism to the effect that it should be made capable of measuring itself in an arithmetical fashion against the liabilities that it has to meet; and this is, of course, a palpable impossibility. What is it, we may ask, that keeps the reserve at its present average figure and no more? It can be nothing else but public sentiment on the subject based on general experience. If there had ruled, during past years, a strong and general feeling in the city that the reserve was in truth dangerously small, the average rate of discount would have been higher than it has been, and the figure of the reserve would then have been higher too.

Such reasoning as this, however, must be accompanied with the proviso that it applies to ordinary circumstances only, and the question may fairly be raised, as indeed it has been:[1] Are the present circumstances ordinary ones? Our immunity from financial panics during the past forty years has been coincident, at any rate, with a state of things in which our navy was, beyond all question, dominant on the seas. Is nothing changed in that respect now, or likely at an early date to be changed? In the past, too, as we have seen, we have always been able, when necessary, to draw money from abroad in quantities that had no obvious limit. The foreigner sent in his gold in millions readily enough, knowing that whenever he pleased he could get it back again. Is it quite clear that, in the new circumstances, he will be as completely satisfied on that point? To the commonly recounted list of services rendered by our navy, must be added that of having in the past secured for us the position of London as the world's Clearing House. No form of public expenditure, indeed, earns a more direct reward for the nation, in actual pounds, shillings, and pence, than the expenditure which is needed to satisfy, not only ourselves, but our neighbours as to the absolute impregnability of our position.

Do we need a War Chest?—This is the first great lesson to which the circumstances of the situation point. Another, as it seems to me, is the desirableness on the part of the nation of losing no time in procuring or accumulating for itself a war chest, a considerable fund in gold altogether separated from the exigencies of finance, domestic or foreign. As things stand at present, who can affirm that it would be impossible that, in the event of threatened hostilities, London might be drained of its gold before a blow had been struck, or even war had been declared. As the *Times* military correspondent tells us in a recent letter, 'The financial preparation for war, not even begun in England, has been concluded in Germany.' Although the gold in the Imperial Bank at Berlin is not practically liable

[1] By Mr. Edgar Cramond in a recent number of the *Quarterly Review*.

to a limitless external drain as ours is, the German authorities think it necessary to keep some £6,000,000 in the national custody at Spandau. An immensely larger sum, as national reserve, is that to which the requirements of the situation point in our case. The nation with which we might be at variance would, of course, take such steps as were open to it to bring about a panic in London. Even if it refrained from this course, however, the hint of possible national insecurity would itself probably be quite sufficient to cause a rush for gold both internal and external, and it might easily prove to be one that would baffle the most far-seeing of calculations.

The Alleged Possibility of Superseding Money.—A question that suggests some interesting reflections is this : In how far is the extension of credit theoretically possible ? There seems little doubt that with increased experience, with a consequent diminution in the liability to errors of judgment, in short, with a more perfected human nature, the substitution of credit for money might safely enough be carried even farther than it has been as yet in England, astonishing as that substitution has been. We find, however, a tendency among a good many of the economists to push too far the idea of the possibility of doing without literal money. When, for instance, in discussing the use of the set-off in place of the money payment, M'Leod remarks that ' the whole system may go on for an indefinite time, and to an indefinite extent without a single coin being required,' he seems either to forget that there is such a thing as retail trade and the wage payments of production, or else to assume an unreal separation between purely monetary transactions and economic life as a whole. Cash, of course, shows no tendency to disappear from retail trade ; rather, indeed, as cities grow bigger and population grows more mobile, the tendency is all the other way.

Mill, again, expresses himself yet more unguardedly than M'Leod. Putting the possible case of a whole nation dealing with one bank only, which, indeed, under our Clearing House and Central Bank system, is, in this country,

not so far from being realised, he says, 'In this ideal case there would be no money anywhere, but in the hands of the bankers, who might then safely part with all of it by selling it as bullion, or lending it to be sent out of the country in exchange for goods or foreign securities. But though there would be no money in possession, or ultimately perhaps even in existence, money would be offered, and commodities bought with it just as at present. People would continue to reckon their incomes and their capitals in money, and to make their usual purchases with orders for the receipt of a thing which would have literally ceased to exist.' Mill, again, plainly forgets that there is such a thing as production, wage payments, and retail purchases. Behind such views of the monetary function lies apparently the conception of credit and of cash as operating in regions that are completely separated from each other. The important truth of their unity of essence, constant interaction, and, at the same time, specialisation of function, are thus left out of sight.

Specialisation of Function between Cash and Credit.—The inadequate degree in which this continual interaction between wholesale and retail money is generally realised is illustrated for us by the stress that is laid by most economists who discuss monetary questions on the fact of the limitation of the legal tender power of silver. In consequence of that limitation, they tell us, silver is not used in large purchases. But is it not? When the shopkeeper, or the publican carries his day's or week's takings in silver to the bank, pays them into his current account, and, on the strength of them, draws a cheque to meet some fresh purchase of stock, does he not practically use silver in large payments? The banks, of course, never so much as dream of refusing to accept it in any quantity in which any one chooses to bring it to them.[1] If they did, the shops, the taverns, the theatres, and the railway companies, would at once find their business brought to a standstill. It is

[1] See Mr. (now Lord) Courtney's evidence before Sir H. Fowler's Committee on the Indian Currency. Reply to question 13,003.

only because the limitation of the legal tender power of silver is absolutely a dead letter that nothing of this sort happens.

We have already noted the fact that, in these days, prices are fixed in practice exclusively in the wholesale trade. In brisk times more retail money is, of course, drawn into circulation than in dull times, but this is the effect, not the cause of the high prices that rule. It is noteworthy, too, that a very considerable rise in the prices of commodities need, as a matter of fact, involve, only a very trifling increase in the quantity of retail money actually in use. The proportion likely to rule between the two is one of those matters that have not, as yet, been adequately investigated. The late Lord Farrer is the only economist who appears ever to have thought of going into the question at all. The quantitative theorists, of course, deal with the subject on the assumption that there is no distinction of any sort between the functions of wholesale money and of retail, of credit and of cash. They conceive that the total amount of money in the country, on which prices are said to depend, can be arrived at if we simply add together the purchasing power that takes the shape of credit, and that which takes the shape of cash. Lord Farrer's line of investigation puts the matter in another light altogether.

Lord Farrer's Line of Investigation.—He obtained in 1887, from Mr. Grierson, the then general manager of the Great Western Railway, some data intended to throw light on the true relations, as regards quantity in use, between wholesale and retail money. These data might, with great advantage, be supplemented, and brought up to date by further inquiry now. He based on them the conclusion, to some extent, of course, a conjectural one, that, while the total receipts of the railways at that date were £70,000,000 annually, and their total outgoings about the same, some £500,000 in sovereigns or notes representing sovereigns were about what was required to do all the railway business of the nation. The Great Western Railway, it was found, sent down, to pay wages and salaries, and to furnish petty

cash, on the average £50,000 a week,[1] eighty per cent. of it being gold, the rest silver or copper. Within the week it was all back again in the bank's coffers.

If Lord Farrer's calculations are approximately correct, which, indeed, there is no reason to doubt, we may base on them the further conclusion that, in the case of the railways, it would require an addition to their annual turnover of about £300 to keep one extra sovereign in circulation, and as railway business involves the use of quite an exceptional amount of cash, we may again conclude that, as regards trade generally, it would need a much larger addition to the turnover to bring about a similar result. It seems clear enough, in these circumstances, that we may leave the quantity of retail money in circulation out of account altogether in inquiring into the determining causes of price variations.

[1] The sums sent down varied between £34,000 and £78,000. See note by Sir T. Farrer on the use of gold on railways. App. iv. to the *Final Report of the Gold and Silver Commission*, p. 93.

CHAPTER XV

ETHICAL ASPECTS OF MONETARY EVOLUTION

We have endeavoured now, after a fashion, to follow the progress of money from its earliest germ in the passion of the savage, first for the shells and the beads, and afterwards for the rings and bangles of silver and of gold that convert him into a thing of beauty in the eyes of his fellows, to the latest complicated developments of modern banking. We can never, indeed, understand any process of evolution till we know it as a whole from first to last. The points that are sensitive to light in the skins of rudimentary organisms appear to us for the first time in their true aspect when we can trace their connection with the retina and the lenses of the human eye. We seem, in such cases, to see the activity of some mind even in the first stages of the evolution busied in bringing about the consummation finally realised in the last.

Works of the Common Mind.—We have in the banking system of to-day an elaborate mechanism, the mere description of which would require a very lengthy volume, and the general features of which are capable of being copied, and indeed are being copied every day by new nations as they come into line with us in economic progress. Yet we know that there is not one of these features the emergence of which can justly be attributed to the inventive genius of any single individual. We might just as well ask who was it that first planned our system of representative and Cabinet government as ask who was it that originally thought out the present organisation of our money market. We seem to be here indeed in the presence of one of those surprising works of the common mind which are full of a still inadequately realised significance.

The salient characteristic of the English constitution, as Bagehot points out, is the union of the legislative and executive functions in Parliament, and in the great committee to which Parliament, strangely enough, entrusts the power of its own dissolution ; yet the separation of the two functions was the favourite project of reform in England at the period of the Revolution of 1688, and only escaped being carried into effect owing to circumstances that present the appearance of being entirely accidental. We see only the impulse towards freedom and self-government active in many generations of Englishmen, and the apparently chance survival of expedients that fell in with the aim of this impulse.

A phenomenon that may perhaps be brought under the same category is the growth of Gothic architecture. 'No one,' as Emerson says, 'can walk in a road cut through the pine woods without being struck with the architectural appearance of the grove . . . nor can any lover of Nature enter the old piles of Oxford and the English cathedrals without feeling that the forest overpowered the mind of the builder.' Yet, if we turn to the history of architecture, we find apparently no one architect who had the design consciously in view of reproducing in stone the image of the forest. We can trace, on the contrary, the various stages by which the basilica became transformed into the cathedral, and can only interpret the ideal that fully realised itself in the fourteenth century as one that, more or less unconsciously, dominated the mind of many generations. The collective continuous mind thus seems to have in it something that cannot be accounted for offhand as the mere sum of the conscious thoughts and wishes of various individual minds.

In his exposition of the theory of Sexual Selection, Darwin seems to think it sufficient to assume that the hens appreciate beautiful forms and colours, in order to account for the fact that the cocks of many species become from generation to generation, more and more beautiful. This indefinite increase in some abstract characteristic called beauty, however, does not at all adequately represent the facts in

individual instances. The 'more and more' can hardly be otherwise viewed than as an approximation towards something in the nature of an ideal existing in some mind that did not itself cease to exist with the passing away of any single generation. How otherwise can we represent to ourselves the gradual evolution of the ocelli on the peacock's tail, or the still more wonderful ocelli that with such incredible accuracy represent the effect of light shining on a convex surface on the wing feathers of the Argus Pheasant? In the difference between the upper and lower ocellus in the illustration,[1] we seem to see the very last finishing touch being given to the picture. Surely we have in such facts as these evidence that is good enough for most of us that there must be somehow, and somewhere, at work in Nature and in man a mind that is not bound up with the cerebration of any single individual.

As regards economic development, the existence of such a mind seemed to our forefathers, and to Adam Smith among the number, altogether beyond question, and the further conclusion that this mind, if it does exist, is on the whole a benevolent one, that, in other words, 'the real tendency of things is good,' is one which, in spite of many appearances to the contrary, a survey of evolution in many of its branches, and not least in the history of money and of credit, encourages us in entertaining.

Money the Root of all Evil.—But is not money 'the root of all evil?' The utterance, it is interesting to note, is not apostolic. It occurs in one of the pastoral epistles, and the pastoral epistles, beyond all question, belong to a period long posterior to St. Paul. It is an outcrop of the same mode of thinking that we find in Pliny when he expatiates on the criminality of the man who first extracted gold from the bowels of the earth and coined it. No doubt money is the root of very much that is evil in the world, but so, for that matter, is sex. Both money and sex, however, belong to the very principle of life in humanity and in civilisation. What a victory, as Nietzsche says, was 'the spiritualisation

[1] *Descent of Man*, vol ii. p. 149.

of the sensuous,' the conquest effected by romantic love of the position it now holds in the thoughts of the men and women of the western world ; and, perhaps, when we have learned not to take the exception for the rule, the current estimate of the moralising value of monetary development may effect a parallel conquest.

Even the curious rudimentary money of Melanesia, a purely indigenous product, has been, we are told, very effective as regards the impulse it gives to the growth of the self-regarding virtues at any rate. There are islands in which every available plot of land is cultivated to the utmost, and a degree of industry displayed never seen in those parts of Oceania where the primitive money is unknown. It is rather, perhaps, in the credit system, however, than in the simple monetary system that we have chiefly to look for the promotion of such virtues as honesty and good faith, for the encouragement of the principles and practices that engrain into the character of a nation the habit of the rigid observance of contracts. Mr. Gilbart, among others, remarks on the manner in which the establishment of banks in countries and localities where they did not exist before, tends to alter for the better the character of large sections of the population.

The Raiffeisen Societies.—In the recent and very interesting development of co-operative credit on the Continent, the operation of the same principle comes out in a most striking manner. The principle of the Raiffeisen societies has justly, as we have noted, been called ' the capitalisation of honesty.' The foundation of each society begins with a small nucleus of peasants who know and trust each other. They co-opt their fellow-members to the required numbers, and, as all are responsible for the debts of any one who makes default, they have evidently the strongest possible reasons for declining to admit any member who is at all likely to do so. The only marvel, in the circumstances, is that the proportion of the peasantry who are ordinarily found admissible, should be so large as it actually is. It becomes a matter of general ambition to be admitted as a member. In many districts,

it is said, there is a distinct tendency on the part of the idle to become industrious, and of the gamblers and the drunkards to forsake their cards and their cups. A certain amount of surveillance of the mode of life of each member by his fellow-members is inevitable, but this apparently seldom results in bitterness or heart-burnings; rather there is a common pride in the success of their 'bank' that tends to cement the society of the whole district,[1] and the remarkable result, as we have seen, is found to ensue, that there is no safer sort of lending than the loans made, under this system, to the very poor.

The coining of the prospective profits of an industry into the ready money with which to carry it on has been, for the alert business man, the great achievement of the English banking system. In Germany and Italy, the development of credit, however, has gone one better, and has enabled the small agriculturist similarly to draw on the future for present cash resources. There is so much in modern progress that has gone to undermine the independence of the poor that here we can very warmly welcome a development that clearly tends in the opposite direction.

Straightness rather than Astuteness wanted.—A survey of the series of steps by which our present system of money and credit has been built up, leaves on the mind the general impression that there has been little room in it anywhere for the ingenious inventor, the man of happy thoughts and clever devices. Rather indeed have such men been the

[1] In Servia the system has caught on with excellent results. The publicans in some instances have been literally frozen out. 'In the village of Mihailovatz,' says M. Avramovitch, the founder of the Servian co-operative banks, 'there used to be two inns; but one had to close its doors at New Year. On one occasion a member of a village bank was seen playing cards, and losing four francs. He was brought before the Committee, and summarily expelled.' With regard to another village, Ozagna, we are told that the Association had 'drawn the people together, and made them friends of one another, as should be the case among honest and well-conditioned folk.' The testimony in this direction is very general. An excellent Catholic clergyman, in regard to a German district, modestly records his opinion that the banks had done more to raise the moral tone of the peasantry than all his own ministrations. See Wolff's *People's Banks, passim.*

originators of departures that have not been durable nor, in the end, useful. It is not so long ago, indeed, that the theorists would have plunged us into all the horrors of silver certificates, or, worse still, of certificates based on the joint security of silver and of gold. Credit has throughout found in straightness rather than in astuteness the source of the influences that have made it grow and flourish. Let a nation steadily recognise its obligations under contracts whether explicit or implied, and that is all that need be asked of it. What we call 'Nature,' it seems, will do the rest. It is, as we know, a familiar truth that London is the only centre in which gold is always obtainable by those who have a right to it, by those who possess documentary promises securing to them payment in cash. This fact, however, means nothing more or less than this, that the Bank of England is the only bank in Europe, or elsewhere, that recognises in a literal and straightforward manner its virtual, if not explicit obligations. It may be very clever on the part of the management of the Bank of France to shield itself from the necessity of making unwelcome payments in gold under the obsolete right to pay in silver, and very cunning on the part of the management of the Imperial Bank of Germany, in similar circumstances, to raise unreal difficulties, but who can doubt that the straighter method has turned out the more politic one as well, in the long-run. We owe to it, as we have seen, the fact that London is now the banking centre of Europe.

In monetary history, England's record has from the beginning been a fairly satisfactory one. Between Edward III. and Elizabeth, no doubt, we depreciated our currency, but to nothing like the same extent as our neighbours. It might fairly be argued, indeed, that such depreciations as did occur in England—up to the time of Henry VIII. at any rate—were forced upon us almost always by the circulation in the country of debased foreign coin. If our own coin had not been occasionally debased, too, it would have been in danger of being all melted down and exported. The Plantagenets never made any money out of their depreciations. It was a remarkable fact that during the period of

our dominance in France in the Hundred Years War, while the French authorities themselves were issuing base money in great quantities, we issued none but the best. In the colonial period in America again, the rule of the English governors was one long struggle with the local authorities against issues of inconvertible paper. Like Philip the Fair, the colonies claimed, as a prerogative of sovereignty, the right 'of debasing and diminishing the money.' The bitterness that ended in the War of Independence was due in no small degree to their continual assertion of this right.

The Implied Contract.—It is worthy of remark in this connection how a State may slide into the position of being virtually bound by a contractual obligation without having ever made the precise contract that nevertheless binds it. The United States to this moment declines to pledge itself in a formal manner to redeem its silver in gold. It might just as well, however, have given the formal pledge long ago. Its statesmen have found it necessary on various occasions to give informal assurances to the effect that it is the settled policy of the country to keep the coins of the one metal on a par with those of the other, and, as a matter of fact, all doubt on that point has long since vanished from the public mind. In India, a quarter of a century ago, while, at the instance of our own theorists, we were keeping the mints open to silver, and allowing the rupee to fall to half its original value, we had nevertheless to recognise, as regards the salaries of our civil servants, that some limit had to be placed to the depreciation. The implied contract was in such a case a serious reality.

To answer the question how it came about that, in the historical development of money, obligations that were in form obligations to pay in silver—as the obligation to pay in pounds sterling is at this moment—became obligations to pay in gold, I would need to reproduce several chapters out of my former book, *The Evolution of Modern Money*. It may here perhaps suffice to say that, as I have endeavoured to show in detail, the present status of gold as the principal money of the world has roots far deeper than it has been

usual to suppose. We know that in the eighteenth century our foreign exchanges were not in the least affected when the silver became light by wear and tear, but responded at once to the attrition of the gold, and recovered at once when the weight of the guinea was restored by the recoinage of 1775.[1] How could that have happened if gold had not even then been the real standard money of Europe, the money of international trade. With regard to France again, in the middle of the sixteenth century, we are told by a contemporary authority [2] that the bankers there made 'their payments and remittances of money to every place in marks, ounces, pennyweights, and grains of gold'; and another authority [3] tells us that after Philip the Fair's depreciations of the silver,[4] the bargains of wholesale trade were no longer made in livres and sols, but in gold. Whatever money is the money of wholesale trade is, in a very true sense, already the standard money. In what other sense, indeed, is gold now the standard of India?

Reality of Obligations under Implied Contracts.—We can note the transition in meaning of the words 'pound sterling' from a given weight of silver to a given weight of gold beginning even in Edward III.'s time. Three gold nobles began then to be spoken of under that designation.[5] By the beginning of the eighteenth century, at any rate, the pound sterling had long left its original reference to silver altogether behind. This perhaps may assist us to realise how bargains that were originally in form bargains to pay in silver, became by the force of circumstances transformed into bargains to pay in gold.[6] At any rate, we can see how real in the affairs of a State may be an obligation, even

[1] Adam Smith, *Wealth of Nations*, book I. chap. v.

[2] Garrault. [3] Leblanc.

[4] The fact is a remarkable one that even Philip the Fair never ventured to tamper with the gold.

[5] *Evolution of Modern Money*, p. 65.

[6] Some curious attempts were made in the mediæval and Renaissance periods to formally adopt the gold standard in place of the silver. They were made in England in Edward III.'s reign (see *Evolution of Modern Money*, p. 70), in France in Henry III.'s (*Ibid.*, p. 110 ff.), and in Florence in 1534 (*Ibid.*, p. 70). The author's view of gold as having been the latent

though it may not be easy to point out the explicit contract from which it arises. The Bank of England now recognises its duties and obligations as the custodian of the country's one cash reserve, though it is not many years since its leading representatives vigorously repudiated them. Facts like these may be worth bearing in mind when we reflect on the tendency of some of our recent legislation. The State, for example, may never have made an explicit contract with the owners of land to treat investments in that form of property in the same manner as that in which it treats all others, but assuredly the implied contract is there, and that being so, its infringement, we may rest satisfied, will bring with it, in the end, penalties that will be exacted to the last farthing.

standard of Europe long before it became the overt standard even of England has been endorsed by Mr. Horace White, LL.D., the best authority in America on banking and currency questions. (See *Money and Banking*, p. 32.)

CHAPTER XVI

THE NATURE OF WEALTH: THE ELEMENT OF ANTICIPATION

THE final section of the first of my chapters on credit [1] was devoted to the consideration of the anticipatory element in wealth, and we were there led to the conclusion that goods that do not at the present moment exist, but that have yet to be produced, necessarily enter largely into our conception of it. Wealth of this description, as in the case of the value of a new gold mine, is found when analysed to be nothing more than the embodiment of guesses and estimates, more or less definite, bearing on events that are yet in the womb of the future. The exigencies of thought and intercourse, together with the play of economic forces in the markets, endow them straight away with an appearance of existence here and now which is to some extent an illusion.

Bearings on the Possibility of Redistribution.—We have, I think, a notable instance of the operation of this illusion in connection with the current conceptions of the national dividend and the capitalised wealth of the country. Calculations have been made which indicate that, in some sense, our total wealth may be set down at something between eleven and twelve thousand millions sterling,[2] and a line of reasoning had been based on them which ends with the conclusion that nothing but the will is wanting to cause us to allot to every British family an income of £200 a year.[3]

The question suggests itself, however, has the conception of wealth itself been adequately analysed by those who put forward such reasoning? Ostensibly, of course, the

[1] Chap. xiii. [2] L. G. Chiozza Money, *Riches and Poverty*, p. 59.
[3] *Ibid.*, pp. 29 and 155.

£11,000,000,000 stands for a given weight of gold, and if it really stood for that, no doubt the sum could be divided up among the population in any manner that Parliament chose to ordain. We know, however, that such a weight of gold exists nowhere. If it is not a weight of gold, however, what is it ? Is it in any sense a quantum or congeries of objects coexisting in time, with a value corresponding to the above figure attached to them ? Such a co-existent quantum is as unreal as the weight of gold itself. The more we reflect on the nature of wealth, the more will we be struck by the fact of what we may call its opportunism ; the fact is, that it is never a mass existing all at once, but always an on-coming series, each item in which may at any given moment be looked upon as waiting for the opportunity of realising itself. Give the things that constitute wealth time, and, no doubt, every shilling of the £11,000,000,000 can be exchanged, if desired, for actual gold, and so, as we express it, can be ' realised.' For this to be possible, however, we must again postulate the condition that, socially, things shall be allowed to go on pretty much as they are going on at present, that the national security shall be maintained, and that the laws shall continue to be fairly well obeyed.

In dealing with the origin of money, I had occasion to observe that the currently accepted theory laid stress on the homogeneity of substance in gold and silver as one of the reasons why early mankind selected them for use as money. We have now further to note the fact—certainly a striking one—that in the extension of money, that is to say, in the extension of the purchasing power of gold to paper and to other commodities through their exchangeability with it, and the practical conversion of these things thus, for many purposes, into money, which, it was found, ensued almost everywhere as soon as property became transferable by document, this homogeneity followed the extension, and came, in a very real sense, to characterise the new repositories of purchasing power, in spite of their endless and infinite varieties of physical attributes. With homogeneity, too, came the conception of arbitrary divisibility.

The fact illustrates the proposition laid down in an earlier

chapter that the things of economics, unlike the things of physics, take their names from their purpose. 'Money,' indeed, seems to begin its career as a name of denotation. The metallic discs which we carry in our purses can be identified for us by pointing them out. Still, even in their case, it might obviously be necessary to explain that they were not intended for the decoration of the person, a use which they largely subserve in the East, and that they were not mere commemorative medals. When we come to the first extension of 'money,' the extension to the bank-note, we find that the conception of purpose takes absolutely exclusive possession of our thoughts. There is not the smallest physical resemblance between five sovereigns and a Bank of England note. That fact, however, does nothing whatever to prevent us from calling them by the same name, and thinking of them habitually as absolutely identical in nature. The same is true of every subsequent extension, and how immensely far-reaching these extensions are we can realise when we reflect that we are not conscious of the slightest inexactitude of expression when we say that the amount of 'money' which a man has left is £1,000,000, though we are well aware that every shilling of it really consists in land, in houses, in racehorses, in shares perhaps, even in doubtful enterprises, so long as they are not bad enough to be devoid of market value altogether. We fasten our attention on their purpose alone, and dismiss all other considerations in regard to them as irrelevant. For us, in respect of their value, these things all become one homogeneous mass. We may proceed to 'realise' them, and divide up the whole volume of value perhaps among a hundred legatees in the ordained proportions. We are led next, it may be, to carry this mode of thinking into our conceptions of far vaster sums, such as the sum of the national dividend and of the national capital, and to assume that they, too, are something homogeneous, and thus capable of redistribution. There, however, the conception assumes the form of an illusion. We can realise any individual estate without difficulty even if the realisation should involve the production of the actual metal, but there

is no known method of realising the national dividend or the national capital, and without realisation, as a possibility at any rate, the redistribution of either is not conceivable.

As money they clearly cannot be redistributed. Can we then fall back on the idea of redistributing the actual things that lie behind the monetary value? A moment's reflection will show us the impossibility of this. The very supposition that the highest incomes in the nation would not exceed £200 per annum, rules out of existence all the wealth that now derives its being from the demand of the rich. Palaces, equipages, Derby winners, old masters, and so on, would be useless to the man with no more than £200 a year, and a family to support out of it. If, however, no one else had more than that amount, then no one could, or would buy such things from the individual who received them in the general redistribution, and thus their value would be found to have completely evaporated. One might as well present a man with a gun from one of the new Dreadnoughts, or a signal-box from the nearest railway station. We may conclude then that the notion of the redistributability of the national wealth takes its origin from the conception of it as a homogeneous mass, which notion again is based on its convertibility into gold, a convertibility which, however, is only possible when time, and, indeed, time without stint is allowed; and which is quite impossible as regards the whole mass at a given moment.

The Wage Fund Theory.—There are several others of the problems of economics on which a fresh light is thrown when we duly attend to this anticipatory character necessarily inherent in wealth. Take the Wage Fund Theory, for instance. We are sensible of the defects of the old line of reasoning which treated the capital of a country as if it possessed a sort of cast-iron rigidity, and thus limited to a hair'sbreadth the amount that could be expended in wages. Shall we then throw it overboard summarily, and accept, with Mr. George, the view that capital has nothing whatever to do with the matter, that wages are paid, not out of capital at all, but out of the product of the wage-earning

industry that is in question ? No doubt cases are citable in which the wage earners wait for their remuneration, or at any rate for a part of it, till their product is sold. Such cases amount probably to something less than one per billion in industry generally. If wages were paid out of the product, and not out of capital, one may ask, how could losing concerns pay them at all, and we know that of the businesses that start every day the proportion of losing ones is very large.

The absurdity of the view is manifest enough. At the same time, if the question before us is this : What is it that limits the amount available for wages in any country ? it seems nearer the truth to answer that it is the prospects of the product, than to answer that it is the amount of accumulated capital. Suppose an Indian reserve in America, or a native reserve in New Zealand is opened up for the first time to settlement. There probably would not be a shilling of accumulated capital to begin with in the district, and there might be none either among the settlers to whom the land was granted. Yet if the land was of the right sort, capital to work it, we know, would not be wanting. Putting aside the case of its introduction by loans on mortgage, sales of holdings, or shares in holdings would introduce it. The prospective income to be obtained from the land would, at any rate, in one way or another, be capitalised, and thus coined into ready money to work it with. If we look at the capital as consisting in material things, ploughs, horses, seed, reapers and binders, and so on, it would be seen largely, no doubt, to come in from outside. But where do the resources out of which such things can be bought come from ? Anticipation of the future appears to bring them into existence as soon as ever the belief becomes general, and becomes well assured that the conditions of profitable production are present. So certain is it that, in these circumstances, the capital to work the land will be present too, that the question of its actual presence seems to become altogether negligible in considering the position for instance as regards the prospects of wages. Increase the certainty of profitable production, and the eagerness to

obtain labour, together with the rate of payment that will be offered for it, will not fail to increase along with that factor alone.

When thus viewed, however, we find that there is a good deal of important truth left in the old theory still. It still remains so far true that wages are limited by capital, that all the wealth which will eventually be paid out as wages must first exist as capital, that, in other words, it must find its way into the pockets of employers before it can find its way into the pockets of labourers. This fact, moreover, points very strongly to the further conclusion that there is no possible method of bringing about a general increase of wages for labour in any country, except that of first bringing about a general increase in the profits of capitalists.

Recovery from Devastation.—The rapidity with which countries or cities recover from a state of devastation due to wars, pestilences, earthquakes, and conflagrations has often, as Mill remarks, excited wonder. He thinks that an adequate explanation of the phenomenon is afforded by the fact of the continual consumption and the continual reproduction of capital. 'The greater part in value,' he observes, 'of the wealth now existing in England has been produced by human hands within the last twelve months.' That is a startling assertion. If it were true then the national dividend would be about one hundred per cent. on the national capital. The real explanation is to be found in the fact of the anticipatory character of wealth, in the fact that capital, as observed in modern business usage, means nothing but 'capitalised presumptive earning capacity.' Once order and security are restored, there is no reason why the same farm, the same mine, or the same mill that used to yield a net revenue of £1000 a year should not hold out a reasonable prospect of yielding it still. If it does, however, it will, of course, itself take rank at once among the items of the national wealth at some figure representing between ten and twenty years' purchase of that income.

CHAPTER XVII

THE CREATION OF WEALTH

Our view of the nature of wealth in the light of monetary theory has led us to some conclusions of practical interest. We may be able to supplement them by glancing at the creation of wealth from the same standpoint.

Walker's Price Theory: its Postulate.—The theory of price determination in vogue among the mathematical economists [1] begins building from the top like the architects of the New York sky-scrapers, but without the steel frame set in a concrete foundation. It takes, to begin with, a price of a given figure for granted, and then asks how its variations upwards or downwards will react on the conditions of demand and supply. This is surely a strange way of explaining the nature and origin of price itself. We have seen that the one economist who endeavours to construct a price theory that really begins at the beginning, is General Walker. His line of thought accordingly is fertile in interesting suggestions. He takes for granted the existence, in a hypothetical community, of a substance that has become the monetary standard, and supposes that, consequently, it is now the aim in life practically of every one to obtain and to accumulate for himself as much as he can of this substance. If Walker does not set all this out precisely in so many words, it, at any rate, underlies as a postulate every line of his illustrative example. 'Wheat, corn, and oats,' he supposes, to begin with, 'exchange for equal amounts of gold, but the farmers soon find that they can raise oats more easily than corn, and corn more easily than wheat, and consequently many farmers bring oats,

[1] See chap. viii.

and much of it, few farmers bring corn, and little of it. No farmers at all bring wheat. Why should they ? Hence, as the existing stock of wheat begins to disappear .more and more gold is offered for wheat until the point is reached when the farmer gets as much gold for a day's work in raising wheat as in raising oats.' Thus it happens, he says, that ' the effort of every dealer to obtain as much as possible of this one article (gold) for each and every part of his stock, the wish of every producer to bring to market the product involving the least labour which will purchase a given quantity of this article ; these must result in ranging all commodities according to the cost of replacing them upon a scale of prices the degrees of which shall be expressed in terms of this one article—money.'

Labour and the Direction of Labour.—It illustrates the solidarity of all the great questions of economics to find that we have here the germ of a theory of price determination, the germ of a theory of cost of production, and the germ of a theory of the creation of wealth. It is in this last aspect that it interests us most at the present moment.

Let us suppose that, in such circumstances as Walker describes, one of our farmers, on taking a survey of his position at the end of his financial year, finds himself in possession of £100 in gold, to what is it that he will be entitled to ascribe that satisfactory result ? ' To the labour,' perhaps you answer, ' that he has bestowed on the ploughing and harrowing of his ground, on the sowing of his seed and the harvesting of his crop. The wealth obtained is the natural reward of that labour.' That is so far true, but it is, obviously, only half the truth. Our farmer might, plainly enough, have worked just as hard as he has worked, and yet have come out at the end of his year with only a fraction of the £100 that he now possesses. Such success as he has achieved is due quite as much to the fact that he has produced the right things as to the fact that he has not spared the sweat of his brow in producing them. If every man had a good angel standing at his side from morning till

evening, ready every moment to tell him to what sort of production he should devote his energies, then indeed we might leave out of account the need for judgment, for foresight and for calculation, as conditions precedent to the creation of wealth, and might attribute the whole result to labour simply. As the world is constituted, we shall find ourselves very far out in our reckoning if we do so.

Here, it must be noticed, a marked contrast emerges between the principles of monetary economics and those of Crusoe economics. The nature of Crusoe's production is dictated for him from the first by imperious bodily needs. Food he must have, and shelter, and in most climates some modicum of clothing. He has no alternative open, and gives, of course, no thought to the question whether he shall produce such things or not, but straight away produces all he can of them. For the man, on the contrary, who is born into a modern organised community, in which exchange has established itself, and in which every one is producing, not for the direct supply of his own necessities, but to meet the requirements of others, and thus to obtain money, success in life depends on producing the things for which there is an outside demand, and consequently in avoiding the production of the things that are likely to be left idle on his hands. The economists, however, very frequently manage to evade the recognition of this fact by their blending of distinct points of view so often referred to in earlier chapters. They represent, as, for example, Marshall does, all wealth creation as the reward of simple effort, on the one hand, and of mere 'waiting' on the other, thus ignoring, or belittling the necessary rewards of judgment and foresight in economic life. Wealth, however, we may be sure, has never in this world been to any considerable extent created by labour, however strenuous, or by waiting, however protracted, without the guidance afforded to production from hour to hour, and from day to day, by eager thought concentrated on the ever-changing conditions of the environment, either directly, by the producer himself, or else by some one under whose direction he is producing.

The Separation of Labour from its Guidance.—In our illustration, adapted from Walker, labour and its guidance remain in the same hands. They are the business of the same individual. The farmer, taken to be a peasant farmer, adapts as best he can the nature of his own production to the changes of the markets. He brings to them less and less of the redundant commodity, more and more of the one that is in demand. All this, however, has, of course, little application to the conditions that rule in the staple industries of the modern world. There, labour is the function of one class, while the direction of it to the right objects is the function of another.

Taking this into account, let us revert for a moment to Walker's illustration, or rather to such a variation of it as is necessary to make it applicable to modern conditions. Suppose the case of a community like our own, in which labour is distributed much as we find it, one considerable section of the working classes being engaged in agriculture, another in the extraction and working of coal and of iron, another in the textile trades, another again in shipbuilding, and so on. In these circumstances let us further imagine that some event occurs that alters at once the whole industrial outlook. Say that war breaks out between two neighbouring nations, and that an urgent demand springs up for battleships, for guns, for armament of all sorts, and again for army clothing, blankets, tinned provisions, for everything, in short, that soldiers need when in the field. Plainly it will be to the interest of our original community that a large proportion of its labour should be withdrawn from other pursuits, and devoted to the supply of these new requirements. How will this diversion of labour take place? Labour itself stands helpless in face of the new situation. The needed change is one which it is completely powerless to effect.

We know, in a general way, how the change does come about. There will be already, of course, a certain number of firms and companies engaged in the production of the commodities which are the subject of the new demand, and of others which are in varying degrees similar to them.

These firms will extend their works, modify their methods, raise fresh capital, and employ additional labour. Besides them again, however, there will be a large body of keen-sighted watchers of the commercial situation, men in possession of free capital, or in a position to command it. They will see their opportunity ; they will build steel mills, establish shipyards, enter on every branch of production, for which the new profitable openings present themselves. Capital at any rate thus flows first into the new industries. Labour mechanically follows suit.

Risk ; its Economic Bearings.—The most careful and far-sighted calculations of the capitalists, however, may, we know, turn out to be at fault. It may happen that while the industrial change is in progress, the warring nations may make up their quarrel. The new demand may die away again as suddenly as it arose, and, consequently, the money sunk in the various forms of fixed capital that were intended to be used in supplying it will, to a large extent, be lost. Such a possibility brings home to us the manifest enough conclusion that the direction of production into the most profitable channels is necessarily attended by risk of the loss of capital, greater or less, as the case may be, on the part of those to whom the function of thus directing it is allotted by the fates. Business risk follows industrial enterprise as the shadow follows its owner.

There is here, it must be said, what Kant might have called an antinomy between the private point of view and the public one. Individual wisdom and public utility in this case by no means necessarily coincide. We see some man who, as we know, is possessed of an income large enough to procure for himself and his family every comfort and every luxury for which any reasonable human being can wish ; yet we find him embarking on some enterprise that we think may, as likely as not, end in impoverishment for himself and for those dependent on him. We are amazed at such folly, and quite justly from our private point of view. The risk-taking spirit, for all that, is the very life blood of economic progress. The world has never yet adequately

recognised the debt that it owes to that class in the community that is always ready to risk the loss of accumulated capital in the hope of increasing it. Eliminate that class, and there would be no new departures in industry; and without new departures where would have been the social progress of the last century, the doubling of the money wages of the labouring classes, together with the cheapening of their necessaries and luxuries? or, looking at the subject in another light, we may ask ourselves what might be the result from the national point of view should we fall behind our neighbours in the race of progress? If we feel that we dare not risk that contingency, the question again presents itself, Is it not just this risk-taking class that keeps us abreast or ahead of them? Japan found it necessary to her continued existence as an independent nation to fall into line with Western ideas, and that consideration was sufficient to overcome in her case the ingrained conservatism of many centuries. Among the national perils that have, of late years, given us ground for grave reflection, none has come home to us with greater force than the discovery that Germany can now build battleships as rapidly as we can, that, in that respect, at any rate, she is now our match, or perhaps more than our match, in the struggle for industrial efficiency.

Mr. Lloyd George, in a recent speech, in referring to a block of mining land in North Wales, had occasion to remark, 'It was perfectly worthless land for agricultural purposes. Why is it now of enormous value? It is because a capitalist comes along and risks the whole of his capital. The capitalist takes great risks with respect to his capital in sinking a shaft. If he does not discover coal his money goes.' Whatever bearing such reflections may have on the landlord question, they express effectively the function of the risk-taker in wealth creation. They emphasise also the necessity for the recognition of the *jus utendi*, *fruendi*, *abutendi* in regard to private property. It is only the man who can feel himself perfectly at liberty to sink his capital in any undertaking that he pleases, how wild and foolish soever it may appear to his neighbours, that is likely to be

able to bring to the light of day the 'ungotten' minerals of a country, or, in other fields of enterprise, to open out yet unthought-of channels for industry. In the case of the Dudley Collieries, to cite the same interesting economist, 'The expert advice was that there was no coal at all, yet the owner insisted on making investigations, and he found a most valuable coal field.' Who cannot call to mind hundreds of instances similar? In regard to the Thames Goldfields in New Zealand, the geologists predicted that not an ounce of gold would ever be found there. Murchison himself, we know, laid it down as self-evident that no gold would ever be found anywhere more than five hundred feet below the surface of the earth. The eager and the rash have always made light of such predictions, and, in the long-run, the result has, to some extent at any rate, justified their heedlessness.

These considerations may be commended to the idealists who imagine that some day all the industries of the world will be run by governments. Do they suppose that the State will ever be allowed to use the tax-payers' money in sinking trial shafts in the wilderness on the chance that gold-bearing stone will be found at the bottom of them? The thing is unthinkable. Nothing is more certain than this, that State enterprise in all conceivable circumstances, and so far as we can judge, even in the very remotest future, will always be subject to very definite limitations. The money that States and Municipalities use is practically trust money, and therefore, in the nature of the case, they must hesitate at new departures; and both the one and the other are pretty certain, if they can, to prevent possible competitors from inaugurating new departures also. The operations of the private capitalist who can do whatever he pleases with his money, are the true motive force of progress in the world, and it is safe to predict that success in the race of life will in the end fall to those communities who do the least to hamper such operations.

Risk-taking and Large Accumulations.—We have noted the antinomy between private wisdom and public advantage

in regard to the risk-taking impulse. The fact seems to point further to the conclusion that the class in the community on whom the function of inaugurating new departures most naturally falls, will be found to be the class who possess spare capital in considerable abundance, the class for whom—to avail ourselves for a moment of the barbarous phraseology of the new economics—the marginal utility of money is lowest. The owner of millions may well, without justly incurring even the imputation of private folly, sink a few hundreds of thousands in floating some new invention, or in building mills or steamships or railways to supply a demand, the permanence of which is, like all things here, uncertain. The strange thing is that he does it. Why cannot he, we might ask, be content to enjoy the ample revenues his millions afford him without troubling himself about increasing them ? That would be the course that hedonistic rationalism would dictate. Fortunately, however, very little of human action is dictated by such rationalism. Our millionaire sees other millionaires who are ahead of him in the race of life, who are greater men than he, and something in his nature impels him to make the attempt to overhaul them, and, if the Fates are propitious, to leave them behind. The nature of his action is instinctive rather than rational. He is, as Von Hartmann would have expressed it, himself ' a dupe of the Unconscious.'

At any rate it may be said that, when we give its due weight to the direction of labour into its most profitable channels, as a condition precedent to the creation of wealth, to ample and liberal risk-taking as a condition precedent to the right direction of labour, and again to the fact of large accumulations of capital, as a condition precedent to the ready assumption of business risks, we will find ourselves impressed with some general conclusions that are calculated to modify the sentiment of hostility so commonly entertained in regard to these accumulations in democratic communities.

In New Zealand, for instance, the sentiment is, or used to be, bitter and widespread ; yet if we ask to what one factor more than to any other New Zealand owes its present great

prosperity, the answer undoubtedly would be—to the frozen meat trade. But who established that trade? Not the peasant proprietor certainly, and, no less certainly, not the State. Its establishment was effected by the enterprise of the New Zealand and Australian Land Company. Sums of money that ran into six figures were lost by the company before the first successful cargo reached the shores of the home country. To no one but a millionaire or millionaire company would such an achievement have been possible.

The Function of the Ordinary Investor.—The part borne by those who assume conspicuous business risks in the direction of labour, and consequently in the creation of wealth, is obvious and unmistakable. The cautious and conservative investor has also his share in the performance of the same functions. The fashion is, no doubt, to represent him as altogether unconnected with the guidance of industry. He is supposed to live on 'unearned' income, and to perform no useful function in the economy of society. At the same time, when we hear of the expansions and the shrinkages of capital, of its movements out of one industry and into another, it is worth while to inquire what these metaphors mean. They mean that human thought in innumerable unpretentious homes is concentrated upon the question how to obtain the best return from savings or from inherited money, and the net result of such deliberations is that this money finds its way largely into the channels in which it can be used most profitably both in the interests of the investors themselves, and of the community as a whole. The cautious investor, like the risk-taking investor, belongs to the system of brain and nerves in the social organism, and is at any rate not less necessary in the complex modern world than the muscles and sinews that are the analogue of labour. When a country is overbuilt, and when fresh building becomes consequently unprofitable, or when a tax perhaps is imposed on the builder's profits, not only is the mind of the builder himself directly affected by the changed circumstances, not only is he led to think

that it is time for him to pause in his operations, but he sees that he cannot go on. The money which he used to find no difficulty in obtaining on mortgage is now not to be had. Why ? Because the cautious investor, in view of the new circumstances, has changed his mind about the desirability of lending it in that particular manner. The cautious investor, no doubt, takes no part in the management of the companies into which he puts his money in the shape probably of preference shares or debentures. He is largely guided, too, it may be, by the advice of his banker, or his solicitor in regard to the manner of its investment ; but if that proves him to be disconnected with the guidance of industry, then we might prove that there is no such thing as popular government, because the ordinary elector is not in Parliament or in the Cabinet, and because he, too, largely relies on the advice of people whom he can trust as regards the manner in which he should exercise his vote.

CHAPTER XVIII

WEALTH CREATION IN THE CURRENT ECONOMICS

In attempting, in the last chapter, to describe briefly the manner in which wealth is created under modern conditions, we saw that there are two quite distinct human factors of which we have to take account,—Labour and the Direction of Labour. We saw, too, that the latter is virtually identified nowadays with the investment of capital. It is through investment, and through it alone, that it operates. Capital flows into new industries first; labour mechanically follows suit. The investment of capital thus stands related to labour in the social organism as the brain and nerves stand related to the muscles and sinews in the human individual. We saw also that the investment of capital is practically always attended with the risk of losing more or less of it, and that its investment in new industries is attended with very great risk indeed. The acceptance thus of such risk becomes an inevitable concomitant of the efficient direction of labour, and, consequently, an indispensable condition of the creation of wealth.

Marshall's Theory.—If my reader is inclined to say to himself that such conclusions as these are obvious truths which it may be worth while to mention, but which it is hardly necessary to dwell upon, I must ask him to take a glance at the account of the same phenomenon, wealth creation, which is set forth in the text-books from which, for the most part, the English student has to glean his conceptions of economic truth. Take Professor Marshall's *Principles*, for example. In the beginning of the work it is laid down that 'economics regards wealth as satisfying wants, and as the result of efforts.' [1] This gives the keynote

[1] *Loc. cit.*, p. 49.

of the system as developed both in Marshall's own writings and in those of his numerous following. The aim is always to show how efforts of a given intensity on the one side are balanced by results of a parallel magnitude in the shape of wealth creation on the other. Jevons, for example, to some extent Marshall's master, draws a horizontal line, and makes a perpendicular descend from it by about half an inch on the under side, and another perpendicular ascend from it by about the same distance on the upper side. The one is said to represent a certain degree of effort involving a certain amount of pain and sacrifice, the other the reward of such effort. The reward of the effort involved in labour we call wages. Wages alone, however, it is admitted, will not account for everything. We must add the reward due to abstinence. Professor Marshall, indeed, prefers to call it the reward due to 'waiting,' [1] but as he defines 'waiting' as the postponement of a present gratification in the hope of reaping a future one, it is really abstinence that he is defining. The change of the expression is a formal, not a real one.

What then is the reward due to this waiting. It is Interest, 'pure' interest unmixed with any compensation for risk, interest, say, at three per cent., which, as it is thought, every one may get without incurring any risk whatever.[2] If any one wants higher interest than this, he must, it is held, incur some risk to obtain it. Consequently, we are to regard the difference between this minimum 'pure' interest, and all higher interest as standing in the place of the insurance premium that is available to cover business risks. A man certainly cannot get any company, or any other individual to insure him against such risks, but he can insure himself against them,[3] and that, it seems, is what he is supposed to do with all that he gets over and above 'pure' interest. Successful voyages, it is said, have to be charged with an (imaginary) insurance premium 'to make up for losses on those which are unsuccessful.' [4]

[1] *Loc. cit.*, p. 233.

[2] Ask, however, those who invested their capital in Consols some twelve years ago, and who have now lost about a quarter of it.

[3] *Loc. cit.*, p. 398.

[4] *Ibid.*, p. 399.

Profits Left Out.—So far we hear nothing of profits. It is felt, however, to be necessary to furnish something that may be taken to be an account of them. The attempt is made accordingly to identify them with 'earnings of management.' This 'earnings of management' takes two forms; first, net; secondly, gross earnings. The latter, as described, presents a very difficult conception.[1] We may take it, at any rate, that both sets of 'earnings of management' are forms of payment for high-class labour.

The theory thus appears to be carefully devised so as to leave out of account altogether what the ordinary man calls 'profits,' the business gain which emerges when a man sells a commodity for a higher price than that which he gave for it, either straight away, or after having subjected it to some process of transformation: Marshall's object, indeed, is confessedly to rehabilitate the Ricardian labour-value theory, while to some extent refining on it.[2] Marx took it up as meaning that the quantity of labour devoted to the production of a commodity is the sole cause as well as the sole measure of its value. Marshall, on the contrary, would hold that the quality of the labour has also to be taken into account.[3] The new form of the doctrine leaves, however, its tenor essentially unchanged. In either form it ignores those aspects of wealth creation which are most difficult to reconcile with socialistic teaching.

This, then, is the backbone of the theory in as far as it is possible to present it within the compass of a few pages. It is not to be supposed that there would be any difficulty in finding *obiter dicta* scattered plentifully enough through Marshall's work that are not readily reconcilable with it. The charm, indeed, of his writings lies in these *obiter dicta*. Let us now very briefly pass in review some of the salient features of the theory.

One form of wealth, Wages, is assigned as the reward of the pain and sacrifice involved in labour. We may let that

[1] *Loc. cit.*, p. 313. The description there given of them might stand as a description of modern civilisation. Their connection with net earnings is indiscernible.

[2] *Ibid.*, p. 503.

[3] *Ibid.*

pass for the present; though we must not forget the work that is done by those who would rather be doing something than standing idle, even apart from the consideration of reward, surely not an insignificant fraction of humanity. Nor must we forget the possibility, and to some extent, indeed, the actuality of the progressive elimination of pain from a large proportion, at any rate, of the work of the world without any corresponding diminution in the vigour and efficiency of production. On this aspect of the subject I have dwelt in a former book, and need not dwell further upon it now.[1]

We come next to Interest viewed as the reward of abstinence, or 'waiting.' We cannot help asking, Would there be no abstinence, no saving, if there were no interest? Would the average man in ordinary circumstances so much as wish to devour his whole substance at one gulp? Would people in general, even if there were no such thing as interest, make no provision whatever for old age, or for a rainy day? To ask the question is to bring out the absurdity of the answer currently given by the theorists. Is there, we may ask, any truth whatever in the assertion that a fall in the rate of interest would make the average man desire to save a smaller proportion of his income than he would desire to save otherwise?[2] Plainly none whatever. Everybody knows that it is when men are getting high interest or high profits that they spend most freely. The attempt to co-ordinate interest as the reward of saving with wages as the reward of labour, is one that will not work. The reward of saving is provision for the future. Interest is thrown in as an added advantage to the saver by the beneficent nature of things. Its own nature and origin, so far as the theory is concerned, remain unexplained.

The Unearned Increment in Elementary Conditions.—Here, it must be said, that we come into collision with the fundamental generalisation of the theorists, the doctrine that the production of wealth is always the reward of effort

[1] *Economic Method and Economic Fallacies*, p. 130 ff.
[2] *Loc. cit.*, p. 234.

or sacrifice. Suppose, to take an elementary example, that a hunter in the uninhabited wilds—as he imagines at any rate—kills a buck that has, say, four times as much meat on it as he can either eat or carry home. He is about to leave the surplus flesh where it is. Suppose, however, that he now learns that he is only a mile or two from a settlement where the meat will be saleable. The theorists would, in these circumstances, apparently, describe the fact that he takes it there and sells it instead of eating or attempting to eat it all himself as 'abstinence.' That, at any rate, is the conclusion that their theory dictates, but it is obviously an absurd one. The new value given to the meat is not the reward of anything in the shape either of effort or sacrifice on the hunter's part. It is, in as far as he is concerned, a piece of sheer good luck. It appears thus that wealth can be created as a result simply of the existence of exchange, and without effort or sacrifice of any sort on any one's part. We thus indeed, probably much to our surprise, come across 'the unearned increment' in these extremely primitive conditions.

We can judge how widespread it is in the world when we reflect that it is hardly possible for a man to produce, or to procure anything for himself with a set intention, without producing or procuring, at the same moment, other things that possess, or may possess, exchange value. The principle in developed conditions is conceived of as the principle of the by-product. You aim at producing cotton clothing, Nature throws in cotton-seed oil. You aim at making gas, you get coke in addition, and so on. The primitive hunter, in our example, aims at satisfying his hunger, he gets surplus meat, and a hide and hoofs which quite possibly possess exchange value. A man lays a net at a river's mouth to get fish for his breakfast, he gets enough fish to supply all his neighbours if they make it worth his while to allow them to share with him. He builds a house, and finds that one of its walls can be made to serve as the wall of some one else's house, if the second man will pay him for the concession. Grant once security of private property, and circumstances will be found to be continually emerging

in which unexpected demand for such property will arise, and will confer upon it unexpected value.

The Neglect of Demand by the Theorists.—In the case of the meat of our hypothetical hunter, we have ascribed its new value to sheer good luck. Another way of putting the case would be to ascribe the new value to the emergence of unexpected demand. The labour-value theorists of all shades concern themselves exclusively with the bearing of supply on wealth production. Demand they treat as a constant, and are content to inquire how this supposed unvarying demand can be best and most economically supplied. They can thus confine their conception of the ability that they recognise to be necessary in modern industry to mere technical efficiency in carrying out processes already initiated, to the sort of ability that is always obtainable on the payment of an adequate salary, and it is thus that they come to identify profits with a form of business gain that is so essentially different from them as the earnings of management, net, or gross, must always be.

Price, Interest, Rent, and Wages are forms of business remuneration that have, no doubt, important distinctions one from another. Still, they are all, obviously enough, species of one genus. They all presuppose the existence of two definite and known individuals, the payer and the payee. They are all fixed sums given for goods, or money, or services, either at one *coup* for a full transfer, or by way of hire for the temporary use. Profits, whatever else they are, evidently do not belong to this genus at all. They are not explicable as a definite payment either for the transfer, or for the use of goods or services. Ordinary speech accordingly refers to a man as ' making ' profits, while it refers to him as earning or receiving wages, prices, interest, or rent. Profits are deducible by the subtraction of price paid from price obtained. They express the outcome of a relation between various forms of contractual payments. To confuse them with such payments would be as absurd as to confuse the angles contained by intersecting straight lines with the straight lines themselves. No one indeed could

fall into such a confusion of thought without a preconceived theory to drive him into it.

Topsyturvydom of the Theory.—When we find profits set forth as being built up out of the various 'elements' of pure interest, insurance interest, and earnings of management net and gross, we have to ask ourselves, Are not the theorists, as in the case of price determination, beginning their theory building at the top, right in mid air? Look at this 'pure' interest, and consider for a moment what it is. It may be the interest on money that is left with the banks, waiting for a more permanent investment, and which, consequently, is lent from day to day for anything that it will fetch. It may be, indeed it most commonly is, money that the State has taken from the taxpayer. Instead of being an element, at any rate, it is always a last result of complex and innumerable transactions. The more numerous the transactions, the more calculable is interest. Once we assume the existence of ordinary shares, we can explain what are preference shares—in various series perhaps—debentures, firsts and seconds, A's and B's, and so on—but the ordinary shares are the necessary basis of the whole structure. We cannot have the preference shares and the debentures without them. We cannot surely regard the return on the latter as furnishing a clue to the elements out of which the return on the ordinary shares is built up. So if we wish to understand the nature of economic payments generally, we have first to inquire into the nature of profits. Once that is understood, the nature of interest, rent, or wages presents no difficulty.

The Primary Meanings: the Right Order.—The one safe guide in entering into an investigation into the nature of any of these forms of gain or remuneration is to take the obvious primary meaning, and to insist on it that it shall be treated as the primary one, and that all others shall be recognised to be what they are, more or less metaphorical and derivative. Adam Smith has much to answer for as the result of his illustration of the apothecary whose high profits on his turnover were really, as he says, to be regarded

as being, to a large extent, wages. It is easy, of course, to understand what he meant, and there is a sense in which such profits present an interesting analogy to the earnings of labour. Still, we must remember that it is an analogy only. It is only by something in the nature of a legal fiction that such profits are describable as wages. In the writings of Smith's present-day followers, these legal fiction payments of wages, of interest, of rent, and of insurance have been promoted to the premier position. The idea is widely prevalent that the rent which a landowner may be imagined as paying to himself, is to be looked upon as the type of rent generally, the only sort of rent which the scientific economist can allow himself to take any note of.

It is, however, quite plain that the theorists here altogether misconceive the essential nature of language. Suppose, to revert to an illustration already made use of, that you see a pile of sovereigns on another man's desk, and are asked to say whether they are interest, rent, or wages, you answer at once : How can I tell what they are unless you tell me first what is going to be done with them ? I must know first whether they are money that you, as borrower, are about to pay to the man who lent you the principal, or whether you, as tenant, are about to pay them to your landlord, or whether you, as employer, are about to pay them to your men. Without this information no one can say what they are. Such things take their names from their purpose. They can have no meaning without the presupposition of the existence of the borrower and the lender, the landlord and the tenant, the employer and the employee.

When we come to Professor Marshall's fictitious self-insurance payments made, as supposed, to cover business risks, the legal fiction method is pushed surely to the verge of the possible. Self-insurance has perhaps some interest for the chartered accountant, but none for the economist. To him it means the same thing simply as forbearing to insure. When it is said that a man debits his successful voyages with the losses of his unsuccessful ones,[1] it stands to reason, of course, that he must do so. Insurance has

[1] *Loc. cit.*, p. 399.

nothing whatever to do with the matter. Profits, as a rule reckoned annually, are a net result after the losses have been deducted from the gains. Imaginary self-insurance might have some bearing on the manner in which the losses are provided for. It can have none whatever on the manner in which the profits are made.

The Blurring of the Profits Concept.—The dragging of it in in this connection merely obscures the true issue. What we want to know is, how does it comes about that there are gains on balance from which losses can be deducted, and this is the question to which no answer whatever is given by all the tiresome theory building that we have been endeavouring to follow out. The answer in brief is, of course, this, that the winner of profits must have gauged the nature and fluctuations of demand with such judgment and such foresight that he has been able first to acquire or produce, and then to sell the merchandise in which he deals at prices that leave an adequate balance in his favour. Judgment and foresight, together with the readiness to accept business risks in reason, these are the essential conditions of the winning of profits, and profits are the basis of every other business payment. It follows therefore, that, generally speaking, the only way of increasing permanently, or over a long period, the volume of interest, rent, or wages is, first of all, to bring about an increase in the volume of profits.

The analysis of profits furnishes us with the business explanation of wealth creation, and it stands, of course, in sharp contrast with the labour-value theory alike of Marx and of Marshall. Mr. Webb, we see, was fairly well justified in his assertion that the Socialists have merely followed the line which the Cambridge economists had traced out for them.

CHAPTER XIX

THE 'UNEARNED INCREMENT'

THE investigations of the last chapter have brought home to us a realisation of the vastness of the sphere that sheer luck occupies in economic life. A great proportion of the wealth that it has been the fashion among the economists to attribute to abstinence, should be attributed instead, we were led to conclude, to simple good fortune. This was the case when the emergence of unexpected demand gave value to that which had none before, as in the instance of the surplus meat of our primitive hunter. In cases of the kind, we seem to be in the presence of that which nowadays would be called the 'Unearned increment.'

The Natural Import of the verb 'to Earn'.—The expressions 'earned' and 'unearned' are, however, expressions which the economist will do well to subject to a careful scrutiny before he freely and confidently makes use of them. The primary meaning of 'earnings' is, of course, the earnings of labour. A man does a week's work for an employer, and gets thirty shillings for it. The thirty shillings are universally described as money earned. We give them that designation simply because they are something transferred from the employer's hand to the labourer's as the result of the services rendered. We do not, in such a case, think of going behind this fact, or of making any inquiries as to the nature of those services. Turn, however, to the use of the same expressions as applied to investments of capital. A man buys a picture, a horse, a block of railway shares, or a block of town land for £100 this week, and sells his purchase for £200 the next. Is the £100 of profits that he has made earned or unearned? It is money that,

as in the case of the earnings of labour, has come into his possession as the result of his own lawful action. Is that fact enough to warrant us in describing it as earned money ? 'No,' say the Single Taxers, and many, or most of the economists. Before we can concede that any money that thus comes into a man's possession is 'earned,' we must know whether his action has been of such a character as to add to the aggregate wealth of the community or not. If it has merely caused the transfer of money from other people's pockets to his own, it is not 'earned.'

Perhaps it is not fully realised that this new conception has been imported into the meaning of the verb 'to earn.' Take, however, any example you please. Suppose that a man buys a property for £10,000, and that subsequently coal is found on it by some one else, and it becomes worth £100,000 ; the difference between £10,000 and £100,000 is said to be 'unearned increment.' Suppose, on the contrary, that, after having bought it, he sinks a shaft at his own expense, and that, as the result of this action, coal is discovered, and it thus becomes worth £100,000, this excess of value over the purchase price is now admitted to be earned. What distinguishes the two cases ? Plainly this, and nothing else, that, in the first, the man's action has made no addition to the aggregate wealth of the community. That addition has been made by some other agency. In the second, the work that he has done, or paid for, has been, at any rate, a contributory cause in effecting it. In the case of the earnings of labour, however, as we saw, we applied no such test. If an operative in a cotton mill was getting thirty shillings a week as wages, we set down his wages as earnings without stopping to inquire whether he was merely living on the waning capital of a losing company, or whether he was really assisting his employer to bring new wealth into the world. It appears thus that we form our meaning for the words 'earned' and 'unearned' on the basis of the earnings of labour, but when we come to employ them in regard to investment, we shift our ground and introduce a new meaning altogether.

The Importance of Right Naming in Economics.—If the question were one merely of nomenclature, we might pass it by without comment, but, as we saw in an earlier chapter,[1] the bestowal of names in economics is never a mere question of words. The assignment of an economic name, on the contrary, carries with it ordinarily far-reaching consequences; and it may be therefore of the utmost practical importance to know whether it is rightly assigned or not. In the present case, to call any business gain 'unearned,' is in practice to say that it is fair game for the tax-gatherer, that it may, at any rate, be appropriated by the State without in any way disturbing the economic life of the community. The same thing is expressed in a variety of other ways. In Marshall's system, if a thing possessing value is held to be a part of the 'Supply Price' of any form of wealth, then it is to be reckoned among the inducements that are economically necessary in order that the exertion should be evoked by which that form of wealth will be created. If it is not part of the Supply Price, or, as otherwise expressed, of the cost of production, then it must be classed among the 'rents,' 'surpluses,' or 'windfalls'; and if you class it among them you virtually say that, whatever other reasons there may be why the State should refrain from seizing it, its appropriation, at any rate, would affect no one but the immediate owner. A tax on 'pure rent,' it is held, falls on the landlord and on him only.[2]

It is evident that this way of viewing the situation, this division of business gains into rents, surpluses, windfalls, unearned increments, and so on, which may with impunity be appropriated by the State, and factors in the Supply Price, which may not, brings us face to face with a conception of the functions of the State which is very different from that which we have been accustomed to regard as normal and legitimate. If we introduce an altogether new principle in regard to a certain class of cases, we will, at any rate, be driven to reflect whether we must not extend it to other cases which appear to be on all fours with them.

[1] Chap. iii. [2] *Loc. cit.*, p. 419.

We may have to ask ourselves, for instance, whether we can say with confidence that the services rendered by butlers, footmen, chauffeurs, yachtsmen, gamekeepers, and all those persons who are engaged in assisting the rich to spend their money, add to the aggregate wealth of the community or not, and if not, whether we must not, for that reason, name them 'unearned,' and penalise them. What again about the singing of unedifying comic songs, of skirt-dancing with the minimum of skirt, of post-impressionist art? Are the earnings of such services in the new and true sense 'earned' or not? Do they add to the aggregate wealth or not? Again, however, why stop at the inquiry whether services literally and immediately add to wealth or not? Is that the only thing to be considered even from the economic point of view alone? Must we not go on to penalise all gains which are the reward of services that cannot be shown to conduce to the benefit of the community as a whole? If we are Ultramontanes, for example, shall we not be led to favour the penalisation of the gains of the Modernist clergy and press? if we are Modernists, of the Ultramontane?

Another consideration again presents itself. Admitting that the really exertion-evoking part of a man's remuneration is to be looked upon as 'earned' money and left alone, we might still have to consider whether he is not getting a great deal more than is necessary to evoke his exertions, whether there is not in his gains a surplus in the nature of 'rent' which might be lopped off without preventing him from rendering the services that he renders now. We might ask, for instance, for how much less than £5000 per annum would Cabinet Ministers consent to perform their important services? Say that they would perform them for £1000; then the question would arise, is not the balance of £4000 'rent,' the appropriation of which by the State would still allow the administration of affairs to go on precisely as it goes on at present? Further examples of a similar character will suggest themselves to the reader. It is plain, at any rate, that any State which would contemplate the consistent carrying out of the principle of penalising the

'unearned' gain will soon find its hands very full of business.

Accepting, however, for the moment at any rate, the definition of the gain that is unearned as that which merely transfers money from one man's pocket to another's, and does not manifestly and directly add to the general wealth, we may yet have to ask whether such gains may not be so closely woven into the texture of economic life that any interference with them by the State may really detract from the progress of the general well-being instead of fostering it. By an analysis of the example of the primitive hunter's surplus meat, we were led to the conclusion that nothing is commoner than to find wealth created by the emergence of unexpected demand for anything that has, no matter how, become the property of any man.

Given the security of private property, and supposing things to follow their ordinary course in this ever-changing world of ours, the unearned gain must be continually making its appearance. For the State to annex it consistently and continually would be tantamount to abolishing private property. To annex it even here and there, would still be a step in the same direction. Reasons, of course, may be adduced in justification of such steps. We have to reflect, at the same time, that the history of civilisation, so far, has been characterised by a continuous growth in the individualisation of property rights as well as a continuous increase in their stability. We have seen, too, how necessary to the most efficient direction of labour is a conception of property so absolute that it sanctions even the *jus abutendi*.

This, however, it may be rejoined, may be true of many forms of property, but not necessarily true of land. It is, however, no less the case with regard to land than to anything else that increasing individualisation of title and security of possession have been uniform accompaniments of progress. Land, however, has, no doubt, peculiarities which have caused the principle now to be well established that property in it is only valid as a claim to compensation. If, however, it is to that extent recognised the important

end of avoiding the disturbance of economic life will be fairly well attained. If it is not, the processes that end in the direction of labour into its most profitable channels may certainly be harassed and impeded.

The Isolated Case Fallacy.—The case indeed is on all fours with many other cases which we have had occasion to notice, in which we have found that in order to view the situation aright, we must look past the single instance immediately under our eyes, and concentrate attention on the general current of events of which it forms a part. For the State to annex profits in a case in which they merely transfer money from your pocket to mine might not be socially injurious if every trace of the annexation could at once be blotted out from the book of fate. That, however, is never possible. Every action, either of a man or a government, must always be looked at as the manifestation of his rule of conduct. What they have done once, they will do again. What they have done in one set of circumstances, they will do in another. The gambler at roulette, who puts his money on the red, may indeed double it, but his added wealth will not increase his credit with any judicious lender. The lender will look to his rule of conduct and reflect that the man who puts his money on either colour will be a bad payer in the long-run. So legislation that infringes long recognised rights of private property may seem to be profitable, but may be dearly bought, although it brings in a few thousands or a few millions in ' windfalls.'

CHAPTER XX

THE RENT THEORY

Rent and Cost of Production.—The distinction on which we dwelt in the last chapter between the 'earned' and 'unearned' gain, dates back to Ricardo's Rent Theory—accepted largely by three generations of economists—which laid it down that Rent does not enter into the Cost of Production. But what can be the meaning of such an assertion? The farmer surely includes his rent-bill along with his wages bill and his seed bill in making up the amount that it has cost him to raise his wheat, and to put it on the market. The difference between the total of these sums and the price that he ultimately gets for the wheat constitutes his profits.

To comprehend how the assertion came, in the first instance, to be made, we must look at the historical circumstances in which it originated. The first we hear of it is in the last quarter of the eighteenth century. There was then a considerable outcry about the high figures to which agricultural rents had risen, and it was commonly maintained that these high rents were the cause of the high prices that ruled for grain, just as it is maintained to-day that mining royalties are among the causes of the present prices of coal. This contention was effectively answered by a Scotsman, Dr. Anderson. Even, he urged, if the land owners lowered the rents that they charged to their tenants to the extent of charging them nothing at all, there would not be anything in that fact calculated to bring about a fall in the price of wheat. Neither the demand for wheat, nor the supply of it would be in the smallest degree affected. The high rents were, he contended, the effect of the high price of grain, and not their cause. Thus the dogma

emerged that changes in rent would not necessarily be accompanied by changes in the prices of agricultural produce; in other words, that 'rent does not enter into cost of production.' In the next generation it was adopted by Ricardo, and became the central feature of his system.

A Transfer of Rents, not a Lowering of Rent.—The answer is obvious enough. The lowering by the landlords of the rents charged to their tenants would not be, in the true sense of the words, a lowering of rent at all. It would merely be a transfer of it from one man's pocket to another's. A similar arbitrary lowering of the wages of existing operatives in existing mills would be in the same position, and would be equally without effect on the price of the product. The same, too, may be said with regard to the interest on borrowed capital. If the lenders handed it back to the borrowers, interest, generally speaking, would not on that account be lowered. The only sort of lowering of the cost of production that tends necessarily to lower the market price of the product, is its lowering all round to every one, and most especially to the new man who thinks of entering the industry. It is a lowering of cost in that sense alone that necessarily increases supply, and unless supply is increased, nothing is done calculated to bring prices down. If you take a case of a real lowering of rent, in other words, of a lowering of the annual value of land—or of the capital value which is essentially connected with it—the case appears in an altogether different light. Such lowerings of rent are often brought about in the world by the annexation of new territory by a civilised power, or by the extension to new lands of facilities for transport by means of steamships and railways. The great industrial fact of the latter part of last century was precisely such a reduction of rent, and, as we all know, it was accompanied by a very conspicuous lowering of the price of grain. Rent thus showed unmistakably in that case that it did enter into the cost of production. Are there not, indeed, at the present moment, hundreds of American farmers passing daily over the border into Canada with no other object than this, that they may

lower for themselves the rent, or what is the same thing, the price that they must pay for land similar to that on which they have been growing wheat in the past ; and may thus reduce, for their own benefit, their cost of production of the cereal.

Marshall adopts the view of Anderson and Ricardo, that the high rents of the early nineteenth century were the effect of the high prices of grain and, plausibly enough, argues that if the rent of land is the effect of the price of the product, it cannot also be its cause. This point needs further elucidation.

The 'Alternative Use.'—Jevons, an acute critic of other people's theories, in dealing with the rent doctrine, puts the pointed question, 'If land which has been yielding £2 per acre as pasture be ploughed up and used for raising wheat, must not the £2 per acre be debited against the expenses of production of wheat ?' Marshall's answer amounts to this, that, in such a case, the rent which land commands as pasture does not 'enter into' the cost of production of wheat, but only indirectly affects it. This distinction, however, is a subtlety that has little interest either for the economist or the practical man. Mill also shows himself alive to the fact that the demand for land for wheat-growing purposes may raise the rent, which those who propose to grow oats on it will have to pay, and so will tend ultimately to raise the price of oats. Mr. Hobson again employs this view of the effect of the 'alternative use' in support of so thoroughgoing a revision of the rent theory that very little of the original is left.

But what, we may ask, is an alternative use ? If the rent that land will command for wheat-growing will affect the price of oats by affecting the rent that will have to be paid for such land as is needed for its production, then will not the rent that land will command for growing, let us say, Tartarean oats, affect the price of common oats for a precisely similar reason ? If that is so, however, can there be any ground for asserting that the rent which one man will pay for land suitable for growing common oats, will not

affect the rent that others will have to pay for land of the same character? If it does, however, the price of the product will, of course, again also be affected. It is plain enough, indeed, that the doctrine of the 'alternative use' followed out to its inevitable consequences, breaks down the Ricardian rent theory altogether.

Rent, like all economic terms, changes its shades of meaning with every change in the context. Because, therefore, high or low rents are the effects of high or low prices of grain, it by no means follows that, from another point of view, they may not also be their cause. If I am thinking of the rent that I, as tenant, at the present moment have to pay, or that I, as landlord, have to receive, I may say to myself, naturally, that its high figure or its low figure, as the case may be, is the effect of the high or of the low price of grain. If, on the contrary, I am thinking of going into the grain-growing industry, I may then say to myself that, with rents at their present figure, I cannot grow wheat at a profit unless I can reckon on getting forty shillings a quarter for it, and if that fact makes me, and others like me, refrain from grain-growing, then undoubtedly the high rents will have checked the supply, and so will have kept up or raised the price of grain. In the first case 'rent' means for me the rent that, as a matter of fact, I am paying or that I am receiving; in the second, it means the rent that other people are willing to pay, and that I will have to pay also if I turn farmer. In the first case, it is a statement of existing conditions that is in question, and such a statement belongs to the past and the present; in the second it is an estimate, and it thus belongs to the future.

The Conversion of Gains into Costs.—The case indeed is only one example of the universal truth that every business gain, once it is established, becomes a business cost to the new man who enters the industry. The great Joint Stock Banks pay dividends of about sixteen to twenty per cent. per annum on their original capital, but if you wish to participate in the profits of such banking, you will not get sixteen to twenty per cent. on your investment. You

will, on the contrary, have to pay such a price for the shares that you will be left with a yield of about four per cent. The moderateness of this yield again, however, prevents the rush of capital into banking that would take place if sixteen per cent. were safely obtainable, and thus helps to maintain the rate of profits in that industry. The case of rent is thus in no sense peculiar. High prices of grain cause high rents. These high rents again prevent an unmeasured rush of capital into grain growing, and so maintain the price of grain. Both classes of facts are thus seen to form part of the machinery by which supply, in the community, is adjusted to demand, in other words, by which labour in production is directed into its most profitable channels.

If, then, we are forced to conclude that high rents may, or, indeed, must, be causally connected with high prices of grain, was Anderson wrong in his contention that even if the gentlemen of Clydesdale had lowered their rents to nothing at all, the price of wheat in Scotland would not have come down ? By no means. The reason has already been given. Rents in the sense of land values are fixed by the conditions of world-wide markets, and are no more liable to be affected by arbitrary reductions in individual cases than the weight of a pound of cheese is liable to be affected by the fact of your putting your hand under one of the scales of the balance.

The Independence of Value.—This fact of the independence of value is one that it is worth while to bear in mind in connection with some recent controversies. When the owners of town properties, for example, are attacked as extortioners because they ask for their shops or houses the rents that are fixed by competition in the open market, we have to remember that if, in any case, they accepted substantially lower rents, they would not be cheapening town lands for the benefit of the public, but would merely, without rhyme or reason, be making presents of their money to the lucky individuals with whom they happened to deal, and who would, no doubt, very frequently realise the gain

at once by passing on the house or the shop at its true value to some one else. The New Zealand Government, misled by theorists, frequently, with the view of cheapening land to intending settlers, was accustomed to fix prices for their rural sections notoriously below the market value; and, in order to prevent them from reaching that value, was accustomed to dispose of them by ballot instead of by auction. They did not, of course, thus succeed, in any true sense, in cheapening land for settlement. The result was that there would often be hundreds of applications put in for one section, and that the drawer of the lucky number would obtain a prize in the State lottery worth perhaps some hundreds of pounds, without, at the same time, having to pay anything for a lottery ticket.

The Marginalist theory is worth glancing at in the light of these conclusions. A man who contemplates entering on any branch of production has, in theory at any rate, the alternative always open to him of buying into a going concern, and paying thus for the natural advantages that have been at the disposal of those who were in a position to make an early choice, or of starting on his own account and foregoing those advantages, while, at the same time, he escapes the necessity of having to pay for them. If he chooses the latter course, and if the industry on which he enters is agriculture, then he would be a taker-up of 'marginal' land, and would evade the payment of rent. To say that this payment of rent, if he decides on paying it, is not part of the costs of production, is thus no more true than it would be to say that the purchase of a mill all equipped and ready for work is a payment that does not enter into cost while the building and equipping of a new mill would do so. As an actual matter of fact, the pioneer is not always—probably, indeed, is not often—the producer in the most disadvantageous circumstances. His venturesomeness is very frequently rewarded by his becoming a producer in decidedly advantageous circumstances. Looking at the matter in advance, however, no one can reckon on getting into an industry except, as it may be expressed, at the 'margin,' that is to say, he must either do without such natural

advantages, at any rate, as are generally known to be natural advantages, or else he must pay full value for them, and in this fact is embodied any semblance of truth that the marginalist doctrine possesses. When the matter is viewed in this light, it becomes very clear that the existence of marginal land, so far from being a cause of the existence of rent for other land, diminishes and restricts it by competing in the market with such other land. This indeed has been pointed out by Wieser and by Marshall.

The Effect of a Tax on Rent.—So much, then, as to the general theory that rent does not enter into cost of production. What next as to the application of it which takes the shape of the assertion that ' a tax on rent ' will fall on no one but the landlord ?

It is notorious that in Canada and in the American Far West, the prospects of enrichment by the rise in the value of the land taken up has frequently, indeed usually, been the main inducement to settlement. The wheat that is grown is often, it has been well remarked, merely a by-product. The real product which the settler looks to as the reward of his labour, his privations, and his risk, is the title-deeds of his property, free from mortgages and other encumbrances. Is it to be imagined then that, in these circumstances, if the Colonial and American Governments had been from the first continually on the alert to appropriate by taxation every increment in land values as it emerged, settlement would have been pushed on as effectively as it has been ? If, however, settlement had been seriously checked, would the prices of wheat have come down as they have done ? What can be more certain than that such taxation of ' rent,' instead of affecting no one but the landowner, would have been at once passed on the consumer ?

Our Increment Duty.—To take another example, and one nearer home. Professor Seligman, in the last edition of his *Shifting and Incidence of Taxation*, cites Mr. Lloyd George's Increment Tax as a case of a tax on ' pure rent,' a tax thus which, according to the theory to which he (Seligman) subscribes, should affect the landowner only.

It may be said that at this point the views of the majority of the theoretical economists, and the views of the majority of practical men engaged in, or connected with, the industries of building and land-development, unmistakably part company. Sir Alexander Stenning, for example, the President of the Surveyors' Institution, in his opening address for 1909, gives it as his opinion, without any hesitation whatever, that 'the ultimate effect of the (increment) tax will be to make houses more costly.' His reasons are that the builder and land developer is 'a man who takes great hazards, including the risk of landing himself in the Bankruptcy Court,' and that 'he expects, and rightly, to have at least the chance of substantial reward. If so large a share of his profits are to be claimed by the State, he must, to protect himself, raise his terms.'

Without complicating the discussion of the subject, for the moment, by introducing the anticipated effect of sales and purchases, let us look, in the first instance, at the question from the point of view of existing owners of land. At any given date, of course, a great deal of the land development and housebuilding of the country will be found to be in process of being carried out directly by those who are landowners at the moment, and a great deal more of it, it may be remarked, will be found to be financed by them for the speculative builder. In these circumstances we know that there will be a certain number of landlords who see clear prospects of large profits to be made by developing and building. There will be, at the same time, a large number of others who would not dream of touching it; and, between the two, there will be the important class, from the economist's point of view, who are weighing the inducements against the drawbacks, and are yet undecided what course to follow. The inducements may be summed up as the returns that will be left to them, from the sale of the houses with the land—whether it be the sale of the freehold or the leasehold—after the costs of developing and building have been fully covered, over and above the amount which they could have got for the land to begin with unbuilt on and undeveloped. The rent obtainable

is usually expected to cover costs or thereabouts. It is the increment in 'pure rent' or site value, and that alone, that is regarded as the natural reward of their trouble and their risk. But if you take away a proportion, say a fifth, of this increment of site value, what can be more certain than that you will deter a certain number of those who are already weighing the chances of loss against the chances of profit from going on with the enterprise. To take 'a strong case,' suppose that you take away the whole prospective increment, it is clear that you will stop building speculation absolutely. You will then leave no inducement to any one to go into it.

So much, then, as to the manner in which the matter stands if we leave the effect of sales and purchases out of account. Is the position in any respect altered if we introduce them? A good many economists take it for granted that the cheapening of land likely or certain to ensue from the imposition of the increment tax must force it into the hands of people who will build on it. But this by no means follows. Professor Seligman quotes, but dismisses without comment, Professor Smart's suggestive observation [1] that, though such a tax would no doubt tend to force the sale of land, yet, 'as the sale would be at a reduced price owing to the impending tax it might force it only into the hands of other and wealthier holders.' This consideration brings home to us, I think, the conclusion that to introduce the effect of purchases and sales does not really affect the question in any way. The new man will simply step into the shoes of the original holder—who will, of course, in his own mind have written down the value of his property—and the line of action that will be adopted by the former will be dictated by precisely the same reasonings and calculations as those which would have dictated the line of action of the latter.

Professor Gonner, in his Memorandum to the Royal Commission on Local Taxation (1899), makes the significant

[1] *The Shifting and Incidence of Taxation*, p. 284 *n.* The remark was not, of course, made with reference to the recent increment tax. It was made some years ago.

remark in regard to that portion of the Inhabited House Duty which might be regarded as being assessed on the site value that it would necessarily 'fall on the ground landlord but for one circumstance, namely, that the tax only arises when the land is put to a particular use.' In that remark we have the true refutation of the theory that such a tax can fall on no one but the present owner. The site is here a mere factor in the production of the thing called a 'house,' consisting of land, bricks, mortar, and so on, and embodying labour, and there is no conceivable reason why a tax on such a factor should not affect the value of the ultimate product. Professor Seligman himself remarks [1] that if we would know whether a tax on anything can be passed on or not, one of the first questions we must ask is the question, Is the thing used in further production or not? The site is here used in further production, and consequently the tax on it can be passed on.

That land is not a reproducible commodity is a consideration that is really quite irrelevant. Its importation into the discussion is due to a confusion between the physical and the economic points of view. 'Tax land,' Mr. Henry George remarks, 'and there will be no less land in the world; but tax machinery and there will be less machinery.' But taxing machinery will not diminish the iron in the universe; it will only prevent some of it from being put to a certain use. So taxing land when it is put to a certain use, which is practically what the increment duty does, though it cannot diminish the quantity of land in the world, can certainly prevent some of it from being put to that use, the use, in this case, of assisting in the production of the commodity called a house.

The general theory, it is hardly necessary to remark, does not limit its application to cases in which a portion, as in the instance of the present tax, a fifth of the increment is appropriated by the State. It asserts roundly that no tax whatever on 'rent' will be felt by any one but the landlord, and, consequently, that if the whole of the increment were taken, no one would be injured except that unhappy

[1] *Loc. cit.*, p. 254.

individual. It is in the nature of the theorists indeed to propound doctrines which would carry them many steps further than even the most unrestrained of practical politicians would be found willing to follow.

Another consideration, again, presents itself. Were even the speculative builder himself as ready as ever, in spite of the recent legislation, to go into building and land development schemes, the facilities that were formerly open to him for obtaining the requisite capital are, in a vast number of cases, open to him no longer. We have it already on the authority of a large number of people engaged in the building trade, that bankers who used to finance builders to a very considerable extent, provided they had sufficient money to provide a fair margin, have practically closed their books, and that it is difficult to sell ground rents at anything like a reasonable price. There seems to be no question that loan money is being steadily driven out of mortgage investments in English land, especially in town land.

But how, it is sometimes asked, can a tax on the increment alone affect mortgage securities ? It will, it is urged, surely leave present values unimpaired. The reasoning is superficial and faulty on various grounds. In the first place, you have only to know the meaning of the word value to know that the present value has a future content. The value of a thing means, indeed, what I will get for it if I put it on the market, and if you lop off so much from what I can, in any circumstances, reckon on getting, is it to be imagined that you will leave the present value unaffected ? In the second place, we know, of course, that the builder or building company enters on its projects fully anticipating that it will make losses as well as profits. If you cut down the profits by so much, but let the losses stand, you will very probably make the man or the company bankrupt, and will, of course, destroy the value of securities.

The Loss of Character by the State.—There is yet another matter to be considered, that is the loss of character by the State. By legislation such as the increment tax and the undeveloped land duty, together with the reasoning by which

they have been supported, every one is set asking, What will come next ? The effect of such questioning cannot be fitted into a mathematical diagram, but it is very real none the less. What, indeed, may not be expected of a State that on one day places ' Mortgages on Freehold and Copyhold land in England and Wales ' on its list of Trustee securities, and on the next adopts legislation calculated to impair their validity ?

If the principles of private law could be applied in the case of the State, the principle of estoppel by conduct would be available to prohibit legislation of the sort. After the State has for hundreds of years sanctioned land transactions as perfectly on a par with transactions in every other form of property, it is surely indefensible to turn round all at once and subject them to unexpected penalties. It seems, however, nowadays to be useless to appeal to principle in matters where the action of the State is concerned. The religious sentiment which, in days gone by, used to be the bulwark of State action in accordance with principle has now, especially among the Nonconformists, among whom indeed it is most alive, gone over to the enemy, and is to be found more often in the Camp of Marat and of Proudhon than in the camp of Edmund Burke. All that one can do in the altered circumstances is to endeavour to demonstrate the connection between cause and consequence, to show the necessity of the conclusion that if legitimate profits in a given industry, under any name, are arbitrarily seized, production, in that industry, will be found in the end not to have gone on precisely as it would have done in less unfavourable circumstances.

CHAPTER XXI

DEMAND IN ITS RELATION TO WEALTH PRODUCTION

The New Emphasis on Demand.—The economists both of the Classical and Mathematical schools have viewed wealth production, as we have seen, mainly from the side of supply. The necessity, however, of viewing it also and equally from the side of demand, has recently been insisted on by several writers. The most important of them are Mr. Hobson, Mr. Robertson, and, quite recently, Dr. Beattie Crozier. The new point of view emphasises the necessity of the expenditure of consumption as a condition precedent to the very existence of wealth. We have been accustomed to think of saving, of thrift, of accumulation as the great creators of wealth. It is clear, however, that, in thus regarding them, we have been looking at one side of the shield only. The expenditure of consumption is undoubtedly that which maintains the values of all commodities at their present figures. If we were to carry thrift to the length of extinguishing such expenditure, or of suddenly and immensely reducing it, values would shrink, and wealth itself would tend to disappear. As Dr. Crozier remarks, saving can only begin when commodities are consumed, or, at any rate, are bought for consumption. In practice, at the same time, we need not worry ourselves overmuch about the danger of under-consumption. That danger was effectively provided against when human nature was constituted on its present lines.

In the preceding chapters we have been led to conclude that the conception of labour as the creator of wealth must be supplemented by the conception of the judgment that directs labour into the right channels, as one co-operating factor, and by that of sheer good fortune, as another. Such

good fortune, however, is present when unexpected demand emerges, and labour is looked upon as well directed when it rightly meets demand. We may therefore change our point of view, and assert that demand itself is to be reckoned among the greatest of factors in wealth production.

The aspects of demand which have been least satisfactorily dealt with in the current economics, are its non-mechanical ones. Professor Marshall quotes with modified approval the striking remarks of Senior on the desire of distinction as an economic force of the first importance. 'Strong as is the desire for variety,' says that economist, 'it is weak as compared with the desire for distinction; a feeling which, if we consider its universality and its constancy, that it affects all men, and at all times, that it comes with us from the cradle, and never leaves us till we go into the grave, may be pronounced the most powerful of human passions.' He supplements it, too, with some interesting observations of his own in a parallel sense. There, however, he leaves it. The conclusions that Senior's reflections suggest do not affect the operative part of his system. The whole marginal utility theory, indeed, is based on the conception of human nature as actuated by motives that spring out of bodily necessities only. The regular descent of the curves as supply increases has reference to the analogy of the satiation of appetite, and to that alone. The theorist of the modern school is led thus to conclude that he can treat demand as a constant, and so need trouble himself little more about it. Hence it comes about that the conditions of supply are those which alone are seriously investigated.

Man as a Factor in a Group.—If, however, Senior is right, or anywhere nearly right, in maintaining that the desire of distinction is the most universally operative of human springs of action, it is surely to be expected that, in the detailed practical discussion of exchange, of value, of cost, and of wealth creation, we shall find that we have continually to reckon with it. Mill, with genuine insight, remarks that if we inquire what is it that we most want, once bodily needs are satisfied, we shall find that it resolves itself into

this, to stand well in the opinion of those about us. A man is always to be regarded as but one factor in a group, never as an altogether solitary and self-sufficing unit. Neither his thoughts nor his actions are comprehensible when we regard him as isolated. The Humist idealism tries to conceive of the manner in which a solitary being would regard the universe. The truth is he would not regard it at all. Consciousness only emerges as the result of intercourse with our fellows. The real, the actual, the objective, in the long-run, mean the things that others can see and feel as well as we ourselves. There is thus a reference to others even in these very elementary conceptions. In the development of the human mind there is a period, as Mr. Sully says, when the child naturally speaks of himself in the third person. He says, 'Charles will go out for a walk' instead of saying, 'I will go out for a walk.' The very conception of the Self seems thus to have for its basis the conception of another. The 'Anders sein' takes precedence of the 'Für sich sein.' In the history of the intellect it will be found that language is the parent of solitary thought, that generalisation, conception, and judgment first become comprehensible when we view them as originating in the exigencies of intercourse.[1]

In economics, too, wherever we look, the solidarity of human groups is borne in upon us; the reference to others is continual. Supply, we have seen, should always be viewed as supply to the group rather than as supply to the isolated individual. I have dwelt above on the important part played by the desire of distinction in the development of money out of ornament.[2] This is but one illustration of the principle. Its influence is universally diffused. We must, however, interpret Senior's expression, 'the desire of distinction' in its widest sense. The same impulse that makes men desire to outrun their fellows in the race of life makes them dread being left behind in it. This aspect of

[1] Practically this is in accord with Lotze's line of thought. Nouns, adjectives, and verbs, in his view, articulate thought into things, properties, and events (*Logic*, book I. chap. i.).

[2] Chap. xi.

the impulse is that which most obviously impresses itself upon us when we reflect upon the effects of supply on demand. Much has been written, and well, about the effects of demand on supply, and about the contrasts presented between its immediate and its ultimate effects. The immediate effect, of course, is to raise prices ; the ultimate effect may very well be to lower them, by eliciting large scale production. When we look at the effects of supply on demand, a parallel result presents itself. The immediate effect of supply is to satiate demand. The ultimate effect may be to create it. Two hundred years ago the wearing of stockings was a rarity in this country,[1] now, as we know, it is universal. In the first instance, the use of them was, no doubt, often attended with discomfort rather than with satisfaction. Scotch country girls not so long ago, in coming into Glasgow or to Edinburgh, used to carry both their boots and their stockings in their hand till they reached the neighbourhood of the town. The supply of stockings, however, to one group in the community gave rise to the demand for them on the part of other groups and other classes, till, in our day, no one practically can be without them.

The Effect of Supply on Demand.—What is it again, one may ask, that maintains the national dividend. Commodities are being produced in ever-increasing quantities, but if there was a consequent continual fall in their value, it is hard to see how the national dividend, as it is called, could be kept up to its existing figure, let alone how it could be kept growing as it does in amount from year to year. We have the answer to the question in the long-period effect of supply on demand. We had occasion to note in a former chapter the manner in which, in the case of armaments, the supply of Dreadnoughts or submarines to one power gives rise to the demand for them on the part of others. Something similar happens in regard to a great number of the requirements of everyday life. Competition, contest, rivalry are, in one shape or another, the breath of life in all things human, just as they are throughout the

[1] The nurse engaged in 1688 for the Prince of Wales possessed none.

lower world. It is relatively only a small part of our wealth that goes to the supply of sustenance, clothing, and shelter. By far the greater part of it goes to the supply of requirements that are dictated to us by the reference to the opinion of others. This all applies to the poor as well as the rich, to a great extent, too, to the savage as well as to the civilised man. I had occasion elsewhere [1] to quote the remarks of a philosophical German traveller, Kubary, on life in the Caroline Islands. In that favoured region every one, with very little labour, could procure all that was needed for the supply of bodily necessities. Was the child of nature then free from the cares that beset us in the modern world? By no means. 'Money [2] plays,' says Kubary, 'a part of the first importance in the life of the inhabitants. The human being, regarded as an animal, has here all that he needs for the support of life. Does he desire to marry a wife, however, to establish a family, to live as a citizen of the State; then he must have money.'

The words 'marry a wife' point us to one great sphere of contest and rivalry, and consequently to a sphere in which the requirements that spring from the reference to opinion, the desire of distinction, and the maintenance of position in life conspicuously present themselves. Among the Irish peasantry marriage is a manifest matter of business. On the Continent, where the marriages are so largely brought about by the relatives of the young people, pecuniary requirements, antecedent to the arrangement of matches, are less disguised than they are among ourselves. Among ourselves even, however, they are of course very real if not so openly put forward. For a young man to be getting on in the world, to have the prospect of being able to maintain his wife and his family in the manner which the sentiment of his class dictates as desirable is, for most men, a necessary condition to their getting wives at all, at any rate, wives of a type with which they could be reasonably satisfied. Maintaining a wife and family in such a manner, however, means, for a great proportion of

[1] *Economic Method and Economic Fallacies*, p. 153.

[2] Their curious indigenous money.

the community, providing housing, clothing, and even food of a character very different from that which would be needed for the mere sustenance of life or even of health and efficiency. Thus the things that had been mere luxuries in one age become converted into practical necessaries in the next. Thus, it may be said, increasing supply operates to create increasing demand, and thus values are maintained, and the figures that represent the nation's and the world's wealth are steadily raised as the years pass by.

Regarded Universally Demand is Insatiable.—A general conclusion which we may formulate as the result of this investigation into the nature of demand, is the following: that, while in individual instances we see, continually, demand being satiated by supply, if we regard the situation universally the case is different. Demand, regarded universally, never seems to be either checked or diminished as the result of increase of Supply. The sum of general demand—in other words, the sum of values—may be likened to a bladder or a cushion half filled with air. If you press it down at one point, you inflate it at others. A half-forgotten nineteenth-century economist, Banfield, justly remarks, 'The satisfaction of every lower want in the scale creates a desire of a higher character.' Jevons, followed by Marshall,[1] would amend the dictum so as to make it run that the satisfaction of the lower want 'permits the manifestation of the higher want.' Practically, the amendment alters nothing. If in either form the statement is true, then it follows that, to represent graphically the general effect of increasing supply on demand, you want, not a descending curve, but a horizontal line, and it will be found that the same applies to the effect of increasing supply on money, the embodiment of demand, and on gold the basis of money.

Identification of Demand with Money.—This view of demand is yet more clearly borne in upon us if we attend to the aspect of it just adverted to, its virtual identification with money. Mr. Hobson, for example, says, 'If we regard

[1] *Loc. cit.*, p. 90.

demand as a power exercised by the purchaser, it signifies and is measured by, an inflow of money.'[1] It will be found indeed that demand in this general sense is essentially a pecuniary concept. If we endeavour to throw ourselves mentally into the attitude of the men of the ante-monetary world, we find that supply and demand taken generally are not distinguishable from each other. They have no general characteristics that differentiate them. If we think of two African natives, A and B, exchanging with each other a bushel of grain for a bushel of salt, the grain appears in the light of A's supply, but it also constitutes the resources behind his demand, and thus, indeed, constitutes its physical aspect. The salt is similarly both supply and demand for B. Our English expressions, supply and demand, tend to make us think that the first is an exclusively physical phenomenon, the second an exclusively psychological one. The French expression *Offre et Demande* are better in this respect. They impress upon us the psychological aspect of both. That they both have a physical aspect is, of course, also manifest. The search for a physical aspect for demand had led many economists to identify it with the quantity demanded, an identification which Ruskin justly repudiates. To follow it out would make the use of ordinary language impossible. It is certain that we can say that the demand for a horse has increased, and it is certain that we do not mean by saying it that the quantity of horse demanded has grown greater. If the physical aspect of demand is to be found in money, and of supply in the things that are offered for money, that fact would validate the opinion of the Roman jurists, that the distinction between buying and selling is an essential and fundamental one, not trivial and superficial, as Mill and so many others of our modern economists assume or assert.

The conclusion that so closely associates demand with money is conformable to the view arrived at in an earlier chapter on quite independent grounds, to the effect that the analogy of the two blades of the scissors is inapplicable to the true relations of supply and demand; that, on the

[1] *The Industrial System*, new edition, p. 170.

contrary, demand lies closer to value than supply does; that it is only possible for supply to alter values by first producing a change in demand, while the alteration in demand operates on value directly, that indeed demand may be regarded as so near to value as to be simply value yet ungraduated. Value, however, in the modern world, we have seen, is an emanation from the institution of money. It can be conceived of as measurable by money, and is quite inconceivable as measurable without it. The three things thus, Demand, Exchange Value, and Money in its extended sense, are really three aspects of the same phenomenon.

Effect on Prices of the Liberation of Money.—Taking this view of demand, Banfield's conclusion that the satiation of lower wants brings into existence higher ones, presents itself in a fresh light. It is seen to be a generalised statement of the truth, often enough commented on, that the cheapening of necessaries liberates money and thus increases the demand for luxuries and comforts. Writing in the *Economist* of the 30th December 1871, Bagehot says [1] that, in 1867, and the first half of 1868, corn was dear (it reached 73s. per quarter). 'From that time it fell, and it was very cheap during the whole of 1869 and 1870. The effect of this cheapness is great,' he remarks, 'in every department of industry. The working classes, having cheaper food, need to spend so much less on that food, and have more to spend on other things. In consequence there is a gentle augmentation of demand through almost all departments of trade.'

The phenomenon continually repeats itself. Virtually, the working classes, in such circumstances, awake at the end of each week, as in Hume's and Mill's fanciful examples, with so much additional money in their pockets. The result, however, is not a meaningless nominal raising of the figures of values all round, as these economists suggest. People, of course, spend no more on the things of which they have enough already. They do spend the money, however, some-

[1] Quoted in *Lombard Street*, pp. 147-148.

how, for the most part. The lower wants being satiated, higher wants, or, at any rate, less mechanical wants emerge. Some people, of course, save the extra shillings, and these saved shillings reach the banks, and are used in production. They help perhaps for the time to raise the price of instrumental commodities, and of their great raw material, iron. What is certain is that, given the existence of fresh resources, the emergence of fresh desires can be reckoned on to create fresh effective demand. This is, of course, a phenomenon of the modern civilised world only, and by no means either necessary or universal. There are, indeed, whole races among whom it hardly manifests itself at all. The Kaffir, when he has earned enough money to buy a sufficient number of wives to keep him in comfort by their labour, resigns himself to a life of ease. With us, however, life is for each individual a round of ceaseless competition from the cradle to the grave, and the desire is practically insatiable for all that will enable each of us to excel in this competition.

The Creation of Conventional Values.—We have already adverted to the reaction of this state of things on the nature of wealth. When all the real wants of human beings are satisfied, the redundant money takes up a rôle of active causality and creates what may be called conventional values. These conventional values all count, however, in the sum of the national wealth. The statistician is not born yet who could form even a wildly conjectural estimate of their total. Real and conventional values are too indissolubly bound up with each other for that. Socialistic and semi-socialistic theorists are fond of dwelling on the vast figures attained by that part of the national wealth that we find in the hands of a relatively small minority as compared with the moderate amount that we find in the hands of the great majority. There is another side to this aspect of the question, however. The very vastness of the amount of wealth in the hands of a small number is itself proof sufficient that such wealth is not of a redistributable character. It must consist either of fixed capital not

capable of conferring direct satisfaction on any consumer, or of the conventional values that are the creation of redundant money, the result of the competition of rich people with each other for things whose main or sole recommendation is that the fact of their possession confers distinction on their possessors.

If we conceive of life as a race, it is plainly not possible for us to think of the State as capable of taking up each unit from the position it has attained in this race, and putting it down again ahead of every other unit. Yet something like this is the ideal aim which the project of the redistribution of wealth, in as far as such wealth embodies conventional and ornamental values, implies. Possible ideals for a nation are the raising of the residuum, the extinguishment of misery, the general diffusion of health, and of education. To act on the fancy that any government can achieve more than this for its people is, beyond all question, to follow a will-o'-the-wisp.

CHAPTER XXII

PHYSICAL AND PSYCHOLOGICAL DEMAND

The Power of Opinion.—The description of demand by a due attention to which so many economic problems are brought for us into a fresh light is, as we have seen, that which is dictated by opinion in our environment. For want of a better name, we may call it psychological demand, as opposed to physical, that which springs directly out of bodily needs. We cannot afford to underrate the deference that, whether we please or not, we are forced to pay to opinion. If a man's or a woman's conduct is so decisively condemned by the whole of his or her entourage as to lead to the withdrawal of the ordinary courtesies of life, and if there is no escape for them from this entourage, then, without any physical penalty, they may find that they have met the worst fate that can befall any human being.

The lower world, it is worthy of note, affords at any rate one curious analogy to this doom of the outcast among men. 'If, by any accident,' says Sir E. Tennant, 'an elephant becomes hopelessly separated from his own herd, he is not permitted to attach himself to any other. He may browse in the vicinity, or frequent the same place to drink in, or to bathe, but the intercourse is only on a distant and conventional footing, and no familiarity or intimate association is under any circumstances permitted.' He becomes a Rogue. 'The emotional temper, or rather transformation of psychology,' says Mr. Romanes, 'which is exhibited by the Rogues here mentioned, is as extraordinary as it is notorious. From being a peaceable, sympathetic and magnanimous animal, the elephant, when excluded from the society of its kind, becomes savage, cruel, and morose to a degree unequalled in any other animal.'

Whether among elephants or men, it is worthy of note that it is the sentiment of those immediately about us that matters, and practically that alone. A wide reputation, fame in the world, is no doubt a very common object of desire, but if we were to look into the matter carefully, we should probably find that it is mainly desired on account of its reflection in the sentiment of those immediately about us. We may remember how, in *Middlemarch*, Mr. Casaubon first feels acutely the realisation that his scholarship lacks greatness when he finds that his wife has made the same discovery. The late Sir Clifton Robinson, in giving to one of our newspapers his views as to the causes of success in life, mentions as one of the most potent in his own experience, affection at home. The man, indeed, who has that, can stand four square against all the buffetings and disappointments of life. May it be long before 'advanced' thinking, which so vigorously denounces competition in other spheres, succeeds in reintroducing it into that one sacred sphere from which Christianity seemed, up till now, to have finally excluded it.

When we hear of some of those sudden conversions that have proved not only sudden but lasting, we will usually have to take account of the fact that the adoption of the new faith, or the awakening to the realisation of the long dormant belief has incidentally been followed by a complete change of the man's environment. From being the most prodigal in a prodigal set, he has now come perhaps to manifest in a superlative measure the qualities that are approved in the new set that he enters. The same vigour of character that made him aim at occupying the most prominent position in the old environment makes him strive to occupy a similar position in the new.

If, again, we could look into the hearts of men, we might, likely enough, find that the leading personage in some obscure sect or coterie—if, at any rate, he can only manage to believe in himself—might be found to enjoy all the rewards that reputation has to offer to mankind in as large a measure as Napoleon after Austerlitz, or as Goethe, Tennyson, or Titian, at the close of their six decades of celebrity.

The Malthusian Theory.—A group of subjects in connection with which the reference to opinion in its bearing on economic theory presents some interesting conclusions, are those that come under the headings of the question of population and the standard of life. It is remarkable that, while Malthus gave Darwin the cue that put him on the track of his great discovery, his own generalisation, as regards the special region of biology with which he was concerned, has not stood the test of verification by the course of events. It is not the case to-day, nor was it, indeed, in Malthus's time, that, in Western Europe, population increases faster than the means of subsistence, and that nothing but vice, disease, and starvation can keep it in check. Even Malthus himself found it necessary so to modify his generalisation as practically to reverse it; and to-day, as we know, the matter on which political thought all over the world is most gravely exercised is not the danger of redundancy in population, but, on the contrary, its tendency to slacken its rate of progress in each community and in each class in proportion as wealth and intelligence increase.

The Fall in the Birth-rate.—The early nineteenth-century economists regarded it as a conclusion that was beyond all question that you had but to increase in any community and in any class the command over the necessaries and comforts of life in order to make population start forward with a bound. What would they have said to the fact that, in our Australian colonies, while individual and family well-being have reached a point seldom, if ever, attained in the world before, the birth-rate per thousand is among the lowest on record? What would they say to the vital statistics published in the city of Providence, in the United States, an important textile centre? They bring out the fact, Dr. Shadwell tells us, not only that the old American stock is rapidly dying out, but also that 'the immigrant races become Americanised and lose their vitality in the next generation'; [1] that is to say, that we

[1] The death-rate there increases while the birth-rate falls. That, however, is the exception. With us, of course, the fall in the death-rate goes far to compensate for the fall in the birth-rate.

have only to raise the individuals of any European nationality sufficiently in the scale of well-being, to doom their stock in a few short years to extinction.

This, it seems to me, is the one cloud on our horizon. In other respects we seem to see reasons for believing that the social forces now in operation are competent to bring about a state of things in which general well-being will be greater and more diffused in the future than it has ever been in the past. But what if well-being itself is inevitably associated with extinction? We can only look about us, and ahead of us, for some development that may put a new aspect on the matter.[1] The gradual cooling of the sun, fraught, as was supposed, with the slow extinction of life, is now, since the discovery of radium, no longer a dogma of the scientists. Possibly the belief in the social doom may show itself to be based on misconceptions, as the belief in the physical doom has done.

In the meanwhile, one satisfactory result of the thought and discussion that have of late years been devoted to the question of race suicide, has been to put a fresh value on the Child in the eyes of the modern community. The advocacy of action based on this fresh value may present itself as one aspect of Socialism, but it is certainly an aspect that attracts many who are not attracted by Socialism otherwise. However little faith one may have in projects for making the poor richer by making the rich poorer, or for making the State do all that is now done by private enterprise, one can cordially agree with Mr. Webb in his contention [2] as to the mischievous absurdity of the system under which we used to permit the casual paupers to drag their children in and out of the workhouses; an evil which, however, it is satisfactory to observe, has been, to a great extent, amended under Mr. Burns' judicious administration of the existing law.

In ruder times than ours, the small and dwindling families

[1] In New Zealand there has recently, as Lady Stout points out in a letter to the *Times*, been a small but still definite rise in the birth-rate. It may, of course, be only an eddy. Possibly it may mark a turn in the tide.

[2] In a Fabian tract.

were liable to be exterminated by the large and vigorous ones, and the desire for children then came to rest on very real grounds indeed. The sentiment survived into a more civilised period. The age-long dominance of law and order, however, has now removed its original basis, and thus weakened it, and threatens to extinguish it. As regards the nation, however, the original grounds still, to some extent, exist. France looks grave at the thought of the German birth-rate, and Germany herself is disquieted at the greater fecundity of the Slav. In the nation, however, the trouble is that the connection between the will to effect a change, and the power to do it has, so far, been lacking ; but granted the continued existence and, perhaps, intensification of the will, the power may, to some extent, ultimately develop itself. The problem, how to forward such a development, is unquestionably the greatest of all those that lie before the nations of the West. To fail may mean to leave the future of humanity to the Mongolian, unless and until he too learns the lesson of race suicide.

The Predominance of Psychological Motives.—The fact that, in all the advanced countries of the world, this great problem is now the subject of continual discussion, and that the conclusion is being everywhere noted and commented on, that the prudential restraint operates in a much more marked manner on the birth-rate among the well-to-do than it does among the necessitous, is calculated to make us modify our conception of the type of motive that is most largely effective in moulding the course of events in economic life. To Malthus or Mill or Ricardo it, of course, appeared to stand to reason that the prudential restraint would operate most on the most necessitous. They would have opened their eyes in amazement if they had been told that that preconception is the precise reverse of the truth. They assumed the omnipotence in human nature of those motives for action, and for the restraint of action that rests on physical needs and the relative insignificance of all others. The same conception of life still survives among their successors. Writers of the modern school will, indeed, as

we have seen, just mention the desire of distinction as a casual matter of interest, but the whole of their operative system, with its strange apparatus of algebraic notation and of diagrams, rests on the analogy of the satiation of hunger only.

They lay it down as axiomatic that, in all circumstances, the marginal utility of money diminishes as the quantity possessed increases. If the marginal utility of money to a man means anything at all, it means the value that he sets upon it. If, then, the axiom were true, it would follow that the fear of loss, or what is about the same thing, of increased requirements for expenditure, would form a stronger deterrent as regards the sort of action that would entail them among the poor than it would among the well-to-do or the wealthy. To this, however, the facts of the birth-rate give a flat denial.

If, indeed, we confine our view to the same individual as seen in varying circumstances, it is no doubt in a large measure true that the fear of such loss as will affect physical needs is a stronger deterrent than the fear of the loss that will touch conventional ones only. If we extend it, however, so as to embrace a comparison between different men and different classes of men, it does not hold good at all. The most reckless of human beings in regard to loss or expenditure is frequently the very poor man who lights on an unexpected windfall, say, for example, the lucky digger who turns up a nugget worth £100. To him the marginal utility of money is at its minimum. For him it stands far lower apparently than it ever does for the average possessor of old wealth. In general literature such a fact as this is always treated as familiar ; in theoretical economics alone, it is denied or ignored. One of our manufacturers, Mr. Russell Rea, brought over some young workmen from Donegal to be employed in work for which bodily strength was the main requisite. They got thirty shillings a week. They had never handled more than half of such wages before. They reckoned consequently that fifteen shillings a week was quite enough for them to bring home to their wives, and the rest they made haste to get rid of in the

public house. To whom could the marginal utility of money be lower ?

In the comments frequently made on the recurrent struggles between labour and capital, it is very generally assumed that the advantage is all with the capitalist. He, it is said, can starve the striker and his family, while the striker at the utmost can merely cause him a loss of income, income which, in many cases, he can well enough spare. In the face of recent events in the industrial world, however, it can hardly be contended that the average capitalist is less amenable to reason, or more likely to allow himself to be carried away by gusts of temper, or by mere irresponsible frivolity than the average workman. The truth is perhaps —so strangely is human nature constituted—that the capitalist, as a rule, dreads loss of income quite as much, and even more than the workman dreads starvation for his family, and, it may be, even for himself. What he has to dread can, of course, in this country, hardly ever amount to actual starvation, though it may mean for him a serious curtailment of necessaries. The ruin of his business, with the loss of his position in life, may undoubtedly for the employer be fraught with as great, or greater, terrors than is this contingency for the workman. The strange thing, indeed, is how lightly and ineffectually the prospective danger to life or limb or health acts on most of us as a deterrent from any course of action to which we are inclined. The prospect of war is found to be the most efficient of recruiting agencies. The difficulty with which workmen in dangerous trades can be induced to take reasonable precautions against the loss of life, or the breakdown of health, is notorious. Alcohol and tobacco owe their popularity probably in very large measure to the danger to health that the use of them is thought to involve. The boy sees his vigorous senior indulge in them, and becomes at once possessed by the desire to do the same, a desire which warnings as to their deleteriousness as likely as not only serve to enhance. Patients in hospitals are known habitually to vie with each other in exaggerating the dangers of their respective maladies, and are hurt if

any one throws doubt on the seriousness of such dangers. The prospect of pecuniary loss, on the contrary, if believed in, never yet, so far as I am aware, possessed for any man any of this subtle charm.

If we ask how was it that Malthus and his contemporaries came to be so far out in their vaticinations in regard to the course that events were destined to follow, the answer is undoubtedly to be found in the inadequate recognition that was accorded in their day, and, indeed, in our own, to those motives of human conduct that we have described as psychological. The reference to the opinion of the group has stepped in, and constituted itself a buffer capable of warding off the operation of the forces that otherwise would have driven population to expand more rapidly than the means of subsistence. The phenomenon is, of course, not only peculiar to humanity, but peculiar, so far, to the humanity of the Western world. In India Malthus's doctrine still holds good. Population continually tends to outrun subsistence. The beneficent work of the English Government loses itself largely in merely bringing more human beings into the world without markedly improving vital conditions.

The Course of Progress in the World.—Progress generally in the world seems to follow some such lines as these. To begin with, nothing but actual obliteration of the individual by death keeps the increase of each type of living being within due bounds. At a higher level foresight comes in, and the fear of death, or of physical injury to some extent, takes the place of their actual occurrence. Fear, again, stereotypes itself in the organism as physical pain. Pain as a rule is the animal's and the child's one premonition of danger. In avoiding it, they often avoid extinction. Turning again to the human and civilised level, we can see an increasing tendency towards the replacement of physical pain itself, together with the dread of it and of death, by the fear of failure in life, the dread of seeing its prizes ravished from us by our competitors. This becomes the really powerful and effective motive of most human action.

If this moral pain can progressively substitute itself for physical pain as a motive of action, then indeed much of that which is most sordid and repulsive in our present environment may gradually find itself eliminated. If we ask, however, whether this moral pain itself may not also, in its turn, be capable eventually of elimination, the case wears a different aspect. Take away pain in every sense, including the bitter disappointment that always attends on failure in every shape, and it becomes hard to see how the pursuit of any serious purpose would be possible, and, consequently, how the human being could fail to sink to the level of the ox in his meadow.

If we could penetrate deeply enough into the intimate nature of things, we should probably discover that a perfectly painless paradise, either in this world or in the next, is as impossible as a triangle whose interior angles are unequal to two right angles. The question touches us practically in connection with the inquiry as to what is the possible ideal for the philanthropist or the statesman. Socialism seems to dream of conditions of the maximum satisfaction for all. As things stand, however, the maximum satisfaction for one man appears to be always and only possible at the cost of the absence of similar satisfaction for another. The conclusion that suggests itself is, that what collectivist writers call the social palliatives are really the only ultimate ends whose realisation is even conceivable.

The reflection, how deeply our thoughts are all penetrated with the conception of the joy that attends on conspicuousness, on distinction, and on competitive success is brought home to us vividly when we see how impossible it is for religious poetry, without relying on this joy and taking it for granted, to depict for us the supreme blessedness of heaven. The saint's crown of glory would be meaningless without some measure of exclusiveness conceived of as attaching to it. Our hymns can only stir the spirit of the worshipper to its depths when they sing of the 'Victor's laurel,' 'The shout of them that triumph ; the song of them that feast,' or of the white robes that clothe the sacred

warriors 'who, with their leader, have conquered in the fight.'

Lord Macaulay, a nineteenth-century Puritan himself at the start of his life, describes in his inimitable fashion the mental attitude of the Cromwellian saint. 'If their steps were not accompanied by a splendid train of menials, legions of ministering angels had charge over them; their palaces were houses not made with hands; their diadems crowns of glory which would never fade away. On the rich and eloquent, on nobles and on priests, they looked down with contempt, for they esteemed themselves rich in a more precious treasure and eloquent in a more sublime language, nobles by the right of an earlier creation, and priests by the imposition of a mightier hand.' In the Apocalyptic conception of the New Jerusalem, even the pecuniary element in beauty is much in evidence. We have it in the gates of pearl and walls of gold, with their foundations of jasper, emerald, sapphire, and amethyst. We seem inevitably to transfer to our dreams of future bliss the ideas of wealth and magnificence, even of social ascendancy, that mould our notions of success in this world.

How Wealth is Disseminated.—The thought of the Puritan saint consoling himself for the absence of a splendid train of menials by the fancy that he was watched over by legions of ministering angels, touches on one outcome of the desire of distinction that is both widespread and interesting. It is worthy of note in how many varying ages and countries the man in possession of superfluous wealth is impelled to surround himself with a train of his fellow-men, and how frequently his importance in the world is gauged by the number that he can, in one way or another, assemble. The Roman Patron, with his troops of clients awaiting his appearance in the market-place, is a familiar example. The baron or knight in the Middle Ages was nobody without his retinue. Among ourselves frequently the first use that is made of increasing wealth by the citizen and his wife as they rise in the world, is to add to the number of their servants, their gardeners, their gamekeepers, and the like; or if they take

to hunting, or yachting, or building, or laying out pleasure grounds, the result is the same, the diffusion of wealth in the shape of wages of labour. If they buy commodities of any sort, a similar result is more indirectly attained. Hence it becomes possible to assert that wealth once created will percolate through every class. By no one was the assertion made with more emphasis than by the late Liberal leader, Sir Henry Campbell-Bannerman. The first aim of the commercial policy, of free traders and protectionists alike, is, and must be, to increase the profits of capitalists. They speak of this very probably as increasing the wealth of the country. But if they wished to be perfectly exact, they would explain that what they hope to do is to bring about an increase of profits, and that they can trust to natural forces to disseminate them. The justification of their trust lies to a great extent in the feature of human nature just noted, the fact that the richer a man becomes, the more he will strive to increase his importance in the world, and that every method of achieving that end leads by one road or another to the increased employment of labour.

We seem here to be in the presence of two purposes, the private purpose of the individual, and the wider purpose of some other mind. A recent writer, Professor Macdougal,[1] justly enough insists on the large share that instinct has in the direction of human affairs. It is instinct, as he says, that furnishes us with all our ends. Reason is concerned merely with the means of carrying them out. Teleological explanations of instinct are, no doubt, out of fashion at present, as, indeed, are teleological explanations of all sorts. Yet surely when we see the mother hen assiduously sitting on her eggs day after day, we do not attribute to her the conscious intention of increasing the population of chickens. Yet that intention must exist somehow and somewhere. This desire of distinction of which we have spoken so much must, I think, be looked on as the instinctive impulse of the individual. Its general end and result we find in the progress of the world, the dissemination of wealth and the raising of social conditions.

[1] *Social Psychology, passim.*

War and Progress.—The connection of war with progress is a subject on which much that is of interest might be written. It is a common matter of comment how barren in mechanical invention was the genius of the classical nations. It is worthy of remark, at the same time, that almost anything in the way of such invention that reached the light of day in antiquity was connected with war, and the preparation for war. The exigencies of war it was, obviously enough, that made the Iron Age supplant the Bronze Age. The lengthened spear of the Macedonians assured their triumph. As with the German needle-gun, the enemy was killed before he could deliver his attack. The grappling irons of the Romans put an end to the naval ascendancy of Carthage. One is struck with the progress of invention when one reads of the wonderful apparatus of battering-rams, scaling-ladders, ballistas, and catapults, which the genial hero, Demetrius the Besieger, brought against Rhodes, and presented to that city once peace was concluded.

At the present moment the great market for the inventor in such things as submarines and aeroplanes, in wireless telegraphy, and even in the latest developments of the steel manufacture, owes its existence to the fact that the nations of Europe are arrayed against one another in hostile camps. The educated man in 1870 proved himself the best soldier. The result has been an immense impetus to elementary education all over Europe. Compulsory service, again, in Germany is coincident, at any rate, with vastly better social conditions than ours, in spite of the existence of a much lower scale of wages, and we are beginning to ask ourselves whether, on social grounds only, we might not gain by adopting it. Here again we seem to see the instinctive blind impulses of the human being—which, at the same time, did not come into existence by accident—made use of for ulterior ends by another intellect than his, one that, it seems, must operate somewhere apart altogether from human cerebration.

CHAPTER XXIII

THE LAND QUESTION

THE Land Question is, beyond doubt, the burning question of the hour in England at present, and failing some great distraction, such as a European war, it seems likely to be a question that will burn with increasing intensity for a good many years to come. Both parties in the State have set before themselves the project of greatly multiplying the numbers of small holdings in the country, whether as freeholds or as leaseholds. It will be the task of statesmanship for a generation to come to effect that object, to repopulate the rural districts, and to do it in such a manner as to cause the least possible disturbance of public confidence.

Land Value Taxation : Varied Grounds of its Support.—The proposal that the unimproved capital value should be made the subject of taxation rests on two very different classes of arguments, and arguments which make their respective appeals to men of very different aims and tendencies. Undoubtedly the backbone of the support which the proposals, as they have been set before us of late, have received, is to be found in the enthusiasm of those who regard land owning in itself as a public wrong, and one that should be set right without a day's delay. That way, of course, madness lies. Support, however, also comes from other quarters. When it is urged, for example, with reference to the vacant sections in a street, that, as they participate with the houses in the benefits of a water supply or drainage scheme—inasmuch as they are thus made capable of commanding a higher rent than they could command otherwise—they should share in the payment for such advantages, we must recognise that we are now face to face

with a different type of reasoning altogether from that of the idealists. The same may be said of the argument that the man who holds vacant land for a rise from year to year, is really similarly situated to the man who steadily reinvests the income that he derives from his stocks and shares. The latter, however, has, of course, to pay income-tax on the sum that he reinvests, and why, it is not unreasonably asked, should not the former also be made to pay in some parallel fashion? The two cases may not, indeed, be altogether on all fours; the reasoning, however, rests on grounds that are apparently sound and businesslike, and certainly embodies no visionary contempt for property rights generally. The same again applies to the reasoning as to the anomalous position occupied by land which has a rateable value of a pound or two per annum, but is found to have a selling value of several hundred pounds. To urge that such an anomaly needs rectifying is, at any rate, merely to urge that land should not be more favourably situated as regards taxation than other forms of wealth, not that it should be made a mark for specially unfavourable treatment.

It would be foreign to my purpose, however, at present to enter in greater detail into the questions of the moment. We will revert again for a little to the general principles that underlie them. There is a good deal of fallacy as well as some truth in the current contention as to the essential difference that exists between land and other forms of wealth. The fact that land so often owes its value to the expenditure of the community is, as has been a thousand times demonstrated, a characteristic which it shares with practically every other form of wealth. When it is urged, however, that the increment of land values can be got at by taxation, while the increment of other forms of wealth almost necessarily eludes us, that is certainly reasoning that is not, at any rate, visionary.

Land is certainly peculiar, too, in respect of the fact that it possesses a degree of stability that renders it possible for it to remain in the same hands from generation to generation, and that thus the increment that accrues to it is liable to become extremely conspicuous. This peculiarity it shares,

no doubt, with certain other valuable objects though with none that are in common use as factors of production of other commodities, certainly with none that are factors in the production of necessaries ; and this peculiarity has had no small share in giving rise to the impression that it is a suitable subject for special taxation.

In my chapter on the nature of wealth, I had occasion to dwell on the fact that wealth consists very largely of things that obtain their value owing simply to the competition of rich people with each other for their possession, desired on account of the distinction which it confers, things, consequently, which could be of no conceivable use to the poor, always supposing the power and opportunity of disposing of them for money to be effectually ruled out. Conceive for a moment how different a place the world would be for most of us if the rich felt themselves impelled to use the vast power which their wealth gives them in such a manner as to absorb a great share of the things that the poor really need, of plain food for example, or plain clothing. Their wealth would then be begrudged to them as bitterly by the masses of their fellow-men as it is at present by a few theorists.

The land of the country, however—not all of it, indeed, but a great part of it—occupies an exceptional position as regards this socially favourable characteristic that attaches to so many others of the objects of desire on the part of the wealthy. It is, indeed, the one point where the desire for display on the part of the rich is liable to clash with the interests of the poor ; and it may thus, of course, clash with the interests of the State too, as undoubtedly it vitally concerns the State to possess a numerous and prosperous country population. It can hardly be denied even by the most conservative among us that the desire of the rich to outshine each other as regards the extent of their landed possessions, does tend to drive up land values, and does thus interpose difficulties in the way of the creation of a peasant proprietary. Among the differences between land and other forms of wealth this, I think, is the one that really counts, and its more or less definite recognition forms

probably the true grounds of the exceptional treatment that land already receives from the community. It has long, as we have seen, been recognised in connection with public works that property in land is valid simply as a claim to compensation, and the same view is coming every day to be more universally accepted in connection with its use for closer settlement. Even Lord Lansdowne, we now find, gives in his adhesion to the principle of compulsory purchase.

Yet another, though no doubt quite a subsidiary, difference between land and other wealth, in this connection, presents itself. With regard to other forms of wealth, we have seen how impossible it is as a rule, even to attempt their redistribution without altogether destroying their value. With regard to land, on the contrary, practical experience has, in a great many instances, shown that it is possible frequently to redistribute it with the ultimate result of greatly increasing its productive power, and consequently its money value. The Cheviot estate in New Zealand, before its purchase and subdivision by the Colonial Government, carried about 60,000 sheep. It carries now, in various kinds of stock, the equivalent of 100,000, besides supporting, at the very least, twenty human beings for every one that it supported at the earlier date.

Is State Landlordism in Prospect?—The interesting question remains to be glanced at:—Suppose we should some day see a scheme of State purchase initiated, what is likely to be the end of it all? Are we marching towards a condition of things in which we shall see the State installed as universal landlord with the cultivators of the soil as its tenants at will? In connection with this question, it may be of interest to revert to the experience of the Colony to which I have so often had occasion to refer, New Zealand.

Shortly after the date when *Progress and Poverty* was published, the premier of New Zealand was Mr. John Ballance. He was a personal friend of Mr. George, and was full of eagerness to give effect to the land nationalising programme. Mr. George, indeed, was sanguine enough to

tell the world that his views were being practically carried out in New Zealand. It has turned out, however, that they were carried but a very little way. One cannot but wonder at first sight why this should have been so. The New Zealand administration did not need to confiscate, or even to purchase the land of private proprietors in order to introduce the system of State landlordism with the retention of the 'unearned increment' by Government. They had vast tracts of valuable Crown Lands in their own possession already. They could further count on a large measure of Conservative support for such a project. A measure intended to initiate it had been already introduced by Mr. Rolleston, a Conservative minister. Why, then, did Mr. Ballance effect so little towards the achievement of his purpose ?

The actual course of affairs ran as follows : A measure was introduced, and indeed enacted, for the purpose of dealing with the Crown Lands under the system of perpetual leases. The leases, though perpetual, left the lands subject to revaluation every seven years. There, of course, came in the State's assertion of its right to the 'unearned increment.' That was all very well. Ministers propose, however, but the forces that we may lump together under the name of the democracy dispose. A considerable quantity of land was taken up by the lessees in perpetuity, and thus a strong interest was soon created in favour of abolishing the provision for revaluation. The members for many country districts soon found that much active and energetic support was to be obtained by making its abolition a feature in their programmes. As for the support that was, at the same time, alienated, it apparently did not amount to much. Very shortly, at any rate, the revaluation clause got itself quietly dropped out of the Act, and the lessees in perpetuity became to all intents freeholders with a quit rent. Many thousands of pounds have since been made by the sale of the goodwill of such lands, and thus the lessees, not the State, have annexed the 'unearned increment.' It appears, indeed, to be a much more difficult thing than any one would imagine for State interests even to hold their

own against private interests in democratic communities. The wholesale overriding of private interests by the State, very often ends mainly in talk. The overriding of the State's interests by energetic private groups appears to be that which, for the most part, really eventuates.

The inauguration of the Perpetual Lease system was followed not long afterwards by that of the Village Settlement system, also under Mr. Ballance's auspices. An Act was passed for the purpose of authorising the grant of small blocks of land—from five to fifty acres in extent—to poor settlers. In this case, not only was the land granted on extremely easy terms, but, besides this, money was advanced by the Government to the settlers, to enable them to fence their land, and to build their cottages. There was every conceivable reason, therefore, to warrant the State in retaining the unearned increment. I need hardly say, however, that it did not long manage to retain it. A revaluation clause indeed, as in the former case, was introduced in the original bill, and became law. Within a year or two, however, of its enactment, it was law no longer. I remember having had the honour of being present at a dinner at which the members of one of the recently established Village Settlements entertained their Parliamentary representative, a genial, though very fiery Radical—he has since attained Cabinet rank—and the occasion proved to be both an interesting and an enlightening one. After the usual vigorous language about the squatters, the member approached a delicate subject, one in regard to which he found himself compelled to differ, as he said, from many other members of the House with whom he was otherwise in sympathy. This was no other than the revaluation of the holdings of the village settlers. He found it difficult to make these town members understand the true position of the poor and struggling pioneer in the country. However, as we know, he and his friends in the end succeeded in achieving this object. The Village Settlement sections were soon as exempt from revaluation as the leases in perpetuity. I have seen the goodwill of some of them selling, about seventeen years ago now, for as much as £12

per acre. No doubt there is a vast deal more unearned increment in them by this time.

In listening to Mr. Hogg, the gentleman referred to, a truth dawned on my mind that has since been abundantly confirmed by the course of events, the truth that, in spite of all the talk about Socialism, the Colony was not really run by idealists of any sort, but by the small farmer and his son, together, we may now add, with his wife and his daughters. The latest news from New Zealand appears to indicate the probability that all the subsequently granted leases, including those of the lands repurchased under the Land for Settlements Act, will follow the course followed by the former ones. The present Parliament is said to be a house of freeholders, both in fact and in sentiment. There appears, it must be owned, something that lies deep in the European nature that makes irresistibly for the freehold tenure.

Altruistic Policies and Egoistic Support.—The lesson to be drawn from such a sequence of events as the above has an application as wide as modern democracy itself. We have found two classes of arguments doing duty among ourselves at present in favour of site value taxation. The phenomenon is by no means a unique one. It finds its parallels indeed almost everywhere in the political and economic sphere. Both the theoretical Socialists themselves, and those who live in continual dread of Socialism, are liable greatly to over-rate its prospects of dominance in the world owing to their omitting to take account adequately of the amount of support which the propaganda receives from the generation that we may describe as Socialists on the make. The description is not meant as vituperative. We are all of us more or less on the make, from the cradle to the grave. We cannot help it, having been made that way. The Socialist on the make, at any rate, lends vigorous and effective support to the idealists for a time, but it is evident that he will go with them only a little of the way on which they propose to travel. In New Zealand the farmers and farmers' sons who wanted hundred

or thousand-acre blocks naturally enough vigorously applauded the eloquence of the land nationalisers, and aided in putting some of them into high office. Now that they have got their land, they applaud no longer.

Support for the idealists comes, too, from other non-altruistic sources. A vast number of people, besides the settlers themselves, have always a direct pecuniary interest in an extension of settlement, and a corresponding interest in preventing its restriction. In Ireland in the 'forties,' when the rural population were leaving the country in thousands, those who left probably, for the most part, bettered themselves. Why then, some have been inclined to ask, should there have been so much bitterness about the matter? Those who put such a question, forget the case of the people who were left behind, the case of the shop-keepers left without their customers, of the abandoned markets, the deserted churches, of the cattle grazing where once there were populous villages. Conversely, when, in the Colonies, there is a prospect of a tract of country held by a few pastoralists, and carrying only their sheep and their shepherds, being converted into dairy farms, let us say, and being thus made to carry a considerable population, hopes of profit begin to present themselves to every one in the surrounding district. The proprietor of the local newspaper begins to see, in prospect, great additions to his list of subscribers and advertisers. The blacksmith, the saddler, the butcher, and the grocer begin to look forward to an influx of new buisness, while the owners of town property dream about seeing it doubled or trebled or quadrupled in value.

Thus it may happen that a policy that, at first sight, looks more or less like Socialism, may be getting ninety-nine per cent. of its support from persons animated by purely egoistic pecuniary motives. The one per cent. of altruists, however, are generally conspicuous out of all proportion to their numerical strength. Theirs are the arguments which the egoists very often listen to with the greatest pleasure when presented in public orations. They can often thus enjoy the satisfaction of fancying themselves

to be animated by altruistic sentiment, while the pecuniary considerations are still operative in the background of their minds ; and thus, in house-to-house canvassing, the latter will often be found the most serviceable. Lord Haldane is probably right in the opinion, recently expressed, that this country will not advance far on the road towards Socialism, simply because the mass of our population are not easily led into courses dictated rather by theory than by practical experience.

CHAPTER XXIV

FREE TRADE OR TARIFF REFORM

THE country gave its answer at the beginning of 1910 to the most difficult of economic problems; and that answer is still an enigma.[1] What alone appears certain beyond all question is that the really deciding conditions in inspiring the verdict of the various constituencies have been geographical ones. Given the position on the map of a borough or a county, and the solution of the complicated problem put before it can, as a rule, be predicted. If it is a cotton-spinning or shipping or shipbuilding centre, dependent in the main on foreign trade, it will probably be found to have made a reply in favour of keeping our present fiscal system intact. If it is a locality engaged in some industry that caters for the home market, it will very likely be all for Tariff Reform. The ambitious politician of the future will first have to select his constituency, in the north or the south as the case may be, and then to select his politics. This state of things finds parallels in abundance in other parts of the world. The Australian landholders, for example, unlike the same class in England or in Germany, have been, for half a century past, whole-hearted enthusiasts for Free Trade, as we can judge from the uniform support given to that cause by their great organ the *Melbourne Argus*; and why? Simply, no doubt, because their principal produce, wool, is practically all of it exported; and because they judge, like the cotton-spinners of Lancashire, that, whatever else Protective Tariffs can do, they can do nothing to assist an export trade. People are hard to convert when their interest stands in the way of conversion, so that we may perhaps conclude that Tariff Reform has now reached,

[1] In view of the attitude of the Irish members.

or nearly reached the limit of the progress that it is destined to make in conquering English opinion.

To some extent, however, it must be admitted that theoretical opinion has altered in the wake of the recent change in public sentiment. Professor Nicholson, for example, up till recently a vigorous and effective champion of Free Trade, comes forward now as a champion of preferential tariffs ; and, all round, there is noticeable a tendency on the part of those who affirm the wisdom of our established system as regards our own country in its actual present conditions as firmly as ever to rest their case mainly on the statistics that tell in its favour, and to let much of the abstract reasoning which did duty in the economics of fifty years ago go by the board. Men, for instance, who are Free Traders from their English point of view, are often found ready to admit that were they Canadians, they would assuredly be Protectionists.

The Consumer as End.—No general statement was in greater favour with the classical economists, or is in greater favour with their successors still, than the statement that our guiding principle should be always and only the interest of the consumer. Production, as they said, was a mere means towards the attainment of an end, and that end was the supply of commodities to the members of the community in the greatest possible abundance, and at the lowest possible price. How, then, could it be right, they asked, to concentrate attention on anything else but on this one ultimate end ? This all sounds axiomatic, but, like most economic axioms, is mainly fallacy. Look for a moment at what we do, and what we think of in any actual concrete case. We are all of us, of course, desirous of seeing employment made more abundant and more regular than it is. We cannot, however, give a moment's thought to any proposal for attaining that end without concentrating our attention on the conditions of production, and on them only. Again, we are in dread, perhaps, of seeing some rival power outrun us in the race for corporate wealth, and thus become able in the end to snatch from us the command

of the seas. Let us hold to Free Trade if we would avert such a calamity, some of us will argue ; let us stimulate our industries by Protective duties, others will urge. Both, however, are at one in looking, and looking solely, at the improvement of the conditions of production as the one and only means of attaining the object at which we are both aiming. Our very national existence indeed is identified with favourable conditions of production. But if this is so, what can be the use of continuing to repeat that the interests of the consumer are the only matter that is worthy of consideration.

It is maintained again by some Free Traders, such, for example, as Lord Avebury,[1] that we cannot injure either an individual or a community by selling them things cheap, or by letting them have things for nothing. This may, indeed, be true universally as regards the individual considered alone, but is it necessarily true, in all circumstances, as regards the community ? Take a hypothetical case. Suppose a small self-sufficing community in which half the population are engaged in producing food, the other half in producing clothing, and suppose further that the surplus clothing is exchanged for the surplus food, and that all get along fairly happily. In these circumstances let us suppose that a millionaire with a turn for experimenting comes along. He makes a present to the food producers of enough clothes to last them for the rest of their lives. Will he not have injured the community ? The clothes producers will have lost their market. Their plant and material will lose its value. They will then either have to starve, or to become dependent on the charity of their neighbours. The 'axiom' omits to take notice of the inter-dependence of the units that constitute the modern community. If they were all self-sufficing individuals, indeed, that had practically nothing to do with each other, then, and then only, would it be true that it would be quite impossible to injure any, or all, of them by giving them things for nothing. The *status quo*, the existing organisation must be taken into account, and anything that disturbs

[1] *Free Trade*, p. 170.

it in too radical a manner can, of course, inflict injury to almost any conceivable extent.

The argument belongs, however, rather to the region of theory than of practice. It is frequently urged, as we know, by the Tariff Reformers that some British industry is in danger from the malignant machinations of the Trusts on the other side of the Atlantic, or of the Kartells of Germany. Whenever they please, it is held, these Trusts and Kartells can crush the English producer by underselling him, and, once he is crushed, they can put up the price of the product again ; so that, in the end, even the consumer does not gain. The answer that any practical Free Trader makes to such an argument nowadays, is not to say that such a thing is theoretically impossible, as, of course, it is not. Something like it is often enough done in private life, though it seems to be too big a thing to attempt internationally. The true answer, at any rate, is not that it cannot be done, that you cannot, in the nature of things, injure a community by selling anything cheap, but that, as a matter of fact, we do not find that it is done, that the true dumping consists, on the contrary, in forced sales by bankrupts, not in the deeply designed operations of unscrupulous millionaires. There is much truth in Professor Sidgwick's view, that Protectionist arguments often appear to have more of abstract theory on their side than those of the Free Trader. It is in their application to the details of practical life that they so often go wrong. Protection, indeed, it may be said, might well have appeared *capax imperii nisi imperasset.*

Consumers again should obviously be divided into two very distinct classes. There is first the poor consumer of the necessaries of life, and his interests are no doubt, in the highest conceivable degree, a legitimate matter of concern to the statesman, both for their own sake, and on account of their reactive influence. There is, on the other hand, the consumer of superfluities, of that enormous class of things, the desire for which springs rather from social reasons than from bodily necessities, and the cheapening of the objects of his consumption is not really, it may fairly be contended, a matter of much concern to any Government,

unless, indeed, it can be shown that its tendency must be to make trade more prosperous generally, that is to say, to react favourably on the conditions of production. The classical economist, however, loves nothing so much as a sweeping, world-wide generalisation. He loves to dilate on the interests of the consumer pure and simple, of the consumer in the abstract, just as if the interests of the consumer of pianos from Berlin, or of costumes from Paris, were necessarily exactly on a par with the interests of the consumers of the food, the clothing, and the shelter that are necessary for health, for efficiency, and for bodily comfort. The truth is, that it is infinitely more difficult to establish an impregnably strong case against the taxation of imported finished goods that partake of the character of luxury or ornament than it is to establish one against the taxation of the food of the poor or the ' materials of industry ' in Adam Smith's sense, whether technically what our Blue Books call ' raw material ' or not.

Expenditure on Imports and on Home Products.—There is, indeed, one Free Trade argument in current use which applies quite indiscriminately to all imported goods of every sort. Leave imports, in all circumstances free, it urges, for this simple reason, that these imports will, in the end, be paid for, not in metallic currency, but in goods which are the product of British labour. That being so, it is urged, it cannot really matter in the least to the country, in the long-run, whether any given sum of money is expended on home products or on imports.

The argument appears, perhaps, cogent on its first presentation. On reflection, however, the question must arise, Does it not prove too much ? After all, it is surely possible to think of cases in which a transfer of expenditure on a great scale from home products to imports could not fail to be in a high degree disastrous to a community, even though it remained true that, after the transfer as before it, imported goods were paid for by exported goods. Take the simplest case possible. Suppose that the owner of an island had a tenantry of small farmers, and that, being a

man of simple tastes, he spent his rents mainly at home, on yachting, shooting, gardening, building, etc. He would necessarily employ a large staff. It might be so large a one that the requirements of its members would absorb the whole produce of the farmers. Suppose again that, on his death, his son was led into spending the money received from his tenants chiefly on foreign luxuries. The staff would, of course, be dismissed, and the farmers would lose their home market. The foreign luxuries would, however, be still paid for, in the end, by the produce of labour in the island, but now, in order to raise the money with which to pay their rents, the farmers would have to sell their produce to outsiders for whatever they could get. Their loss would thus be brought about by the fact of their being deprived of the home market which had sustained the value of their produce ; and the possibility of similar loss cannot in any circumstances be left out of our calculations, nor can it be refuted by the demonstration of the undoubted fact that imports will still be paid for by exports.

The argument apparently would prove that the growth of absenteeism could inflict no injury on any country. It appeals to the theoretical economists with more force than it would otherwise, owing to their conception that the right way to view commercial transactions is always to regard them as cases of barter pure and simple. The imports in their view represent one side of an exchange, and a corresponding export is its inevitable sequel. Each particular import is therefore frequently conceived of by them as the definite cause of some particular, though unknown export. The imports thus, it is held, cannot possibly be increased without bringing about a precisely equivalent increase in exports. That the two are very generally found to increase together is undoubtedly true. The Euclid-like presentation of the reasoning is, for all that, not satisfactory. Causality can never be safely predicated in economics, unless we can see every step of the process. As regards raw materials and ' half stuffs,' the precise manner in which their unrestricted importation operates to bring about increased exports can, indeed, often be shown in detail. It lowers the cost of

making the finished product, and thus enables its makers to compete successfully with the producers of foreign goods in neutral markets. As regards finished goods, however, is it possible to affirm that any similar mode of operation is always, or anywhere visible ? If we buy German toys, or German pianos, it may indeed be argued that we make the Germans richer than they would be otherwise, and thus make them able to buy something from us in return, that they could not buy otherwise. If they do not do this, but spend the money instead elsewhere, then it can further be argued that they make some one else richer, and that he will spend his added riches on our produce. But will he ? The reasoning surely seems to lose its convincing character when we view the world's commerce as it really is, as a series of sales and purchases for money, not, as the text-books idly represent it, as a series of exchanges in kind.

The Conclusion to which the Reasoning really Points.— Still, after all is said and done, perhaps we will find that it is rather the form than the substance of the argument that is at fault. It may be that it points to conclusions very much less definite indeed than those which it ostensibly affirms, but which are yet of the highest importance. If we were to attempt to affirm with regard to machinery that for every unit of labour which a given machine might displace, it must of necessity provide employment for another unit, we should find it very difficult to demonstrate the truth of our assertion. Yet, for all that, the hostility to machinery, on the part even of the labouring classes in all civilised countries, though still an undesirable influence in industry, is assuredly on the wane ; and this is, no doubt, due mainly to the fact that, on a general view of industrial conditions in the world, it becomes clear that where machines have been most widely adopted, there the demand for labour is not least, but greatest. This result is so familiar to us now that we do not realise how marvellous a paradox it involves. All over the world we find the strongest brains of the race continually at work on the problem how to save labour. We see the capitalists and their managers turning

over in their minds, day by day and year by year, all the possible mechanical devices by the adoption of which they may be able to dispense with a hundred men in one department ; or, perhaps, all the possible changes in organisation, such as amalgamations with rival firms, by which they may be able to dispense with a thousand men in some other. Yet the result in the end is that more men than ever find themselves at work, and, on the whole, at better rates of pay than heretofore. The perception of this fact is vaguely but, at the same time, very widely effective in driving home the lesson that it will always be wise for us to think twice about interfering with any development which makes for reducing the cost of production. Unpopular as the Trusts are in America, the ablest statesmen there are vividly impressed at the present moment with the danger of putting the Sherman Act into operation in such a fashion as seriously to check the great accumulations of capital under the direction of a single mind which so manifestly make for the reduction of costs, and consequently for the promotion of industrial efficiency in the nation. Beyond all question, the unrestricted importation of human food, and of the materials of industry, make no less infallibly than improved machinery, or amalgamations of rival enterprises for a similar reduction ; and this consideration has apparently been the principal factor in inspiring the determination on the part, both of masters and men, in so many of our great industrial centres to see to it that it shall continue unimpeded. There is one large sphere, indeed, that of transportation, in regard to which the operation of unrestricted imports, and that of mechanical invention are rather to be described as identical than as merely parallel. Both tend to furnish us with foreign material at lower prices than those at which we could get it otherwise. So that when we remove duties from imports we seem, as a rule, to be placing ourselves in line with the general trend of progress in the world.

Convergence of Contradictory Ideals.—It is remarkable, indeed, that when we regard industrial conditions from one point of view, that which inevitably presents itself to us as

the end by all means to be attained, is the economy of labour. Regard them again, however, from another point of view, and we find ourselves driven to consider by what means it may be possible to increase employment in a country, literally to 'make work' for those who want to work. Without work in fair abundance certainly no population can be reasonably happy, and no State can thrive and become great. Bastiat and writers of his type were very much alive to the validity of the first ideal, but less so to the equal validity of the second. It is true, indeed, that if we were to jump at all and every conceivable means of making work, we should fall into the absurdity of wishing for less daylight in the interests of the candlemakers, or of enacting, like our fathers, that corpses should be buried in woollen cloth in the interests of the graziers and weavers. Suppose, however, that we hope to 'make work' by land legislation that may tend to bring about the conversion of pasture lands into dairy farms and market-gardens, the matter stands in another light. The dominant problem, indeed, in the minds of most of the statesmen in the world at the present moment is that of 'making,' in one way or another, more 'work' for the population of the lands that they rule. The wonderful thing is that in practice the two contradictory ideals seem to converge. Very frequently, at any rate, the more that we can economise labour and reduce costs, the more abundant does employment become.

It must, at the same time, be admitted that reasoning of this type points to conclusions in favour of making Free Trade our general guiding principle rather than to the definite affirmation that nothing but Free Trade can ever be desirable. No one, of course, dreams of basing upon it the inference that import duties are to be condemned universally. The taxation systems of almost all civilised nations already embody the principle of taxing such commodities as are held to be more or less deleterious to the national health, alcohol in all its forms, for example, as well as tobacco; and I do not know that there is any valid reason why the same principle should not be extended so as to bring within the tax-gatherer's ken commodities that,

from the point of view of health and comfort, are practically useless. The imports of the Tudor and Plantagenet days were, for the most part, of this character, silks, velvets, spices, and so on, and this is a fact which we should bear in mind when we are inclined to condemn or to laugh at the old economists for their lamentations over the loss of the country's treasure which such imports tended to bring about.

It is, I think, also putting an undue strain on the Free Trade principle to draw from it the conclusion that a national government or a municipality necessarily does what is altogether foolish and useless if, in allotting its orders for plant or material, it favours in any degree the home producer when in competition with the foreigner, or varies by a shade from the rule of always buying in the cheapest market. To validate such a conclusion, it would be necessary that we should be able to feel perfectly satisfied that every import necessarily causes a precisely equivalent export, and we have come to the conclusion that this, though it is often asserted, is by no means demonstrable. Altogether, perhaps the sound conclusion is that while we would make no serious mistake in adhering throughout to the principle of taxation for revenue only—and as little of that as possible—there is yet a borderland where the question of the imposition of duties with more or less of a Protective tendency is, at any rate, arguable. If it were found, for instance, that the reimposition of the shilling per quarter registration duty on corn, with remission in the case of imports from British possessions, would have a markedly favourable effect on colonial sentiment, we should perhaps be unwise to refuse that concession. Its effect on Home prices would be altogether negligible. At the same time, it cannot be denied that such a course would be very like playing with fire. Before dreaming of its adoption, we would do well to satisfy ourselves that it would not cost us the loss of the most favoured nation clause in the tariffs of the United States, of Russia, and of the Argentine Republic, to mention no others. We should like to know, too, that America would not prohibit the transit of Canadian

wheat through her territory in bond, nor think of retaliating upon us by an export duty on cotton. We are at her mercy apparently if she regards the provocation as sufficient.

Again, as to such proposals, it seems to me that our agrarians would do well to consider not only what the tax on grain will be likely to effect, but also what it will infallibly get the credit of having effected. Wheat has now been steadily on the rise for several years past without any protection, mainly because the rapidly increasing population of the United States is every year consuming a larger and larger proportion of its own supplies. If this process continues, as very probably it will, bread will probably in the near future become quite perceptibly dearer than it is now, and, at the same time, agricultural rents will rise. If all this should happen, however, nothing is more certain than that the Protective tax, small as it may be, will get the full credit of having caused the whole of the rise in both bread and rents, and that the enthusiasts for the application to land of confiscatory taxes will find their hands strengthened and their numbers augmented.

Among the other Protective taxes for which a passable case can be made, is that of a duty on hops. Hops are, no doubt, a material of industry, but then it may fairly be contended that the industry is not one which we need be overwhelmingly anxious to encourage, while, at the same time, there are few things that would do so much as the revival of the hop culture to check the depopulation of the countryside. If the outcome of the discussions on the subject should be the appointment of a Royal Commission to consider the whole question, that proposal is certainly one that should come within its purview.

Imperial Consolidation.—As regards Imperial consolidation, the suggestion continues to be made—it is made by Professor Nicholson, for instance, in his recent book, *A Project of Empire*—that the adoption of a preferential Tariff policy now may lead up, in the end, to the establishment of inter-imperial Free Trade, of a true British Zollverein. It is no exaggeration, however, to say that opinion

in the self-governing colonies themselves scouts such suggestions in the most decisive manner conceivable. It is, perhaps, a little curious that this should be so. Undoubtedly it would be a serious detriment to the young colonial industries to be exposed to the competition of our highly developed ones. But a parallel objection to that applies to all consolidations. The competition of Prussian industries could not have failed to injure the industries of Bavaria, yet that did not prevent Bavaria from accepting the Zollverein, nor from accepting with enthusiasm the subsequent unification of the German Empire which fixed it in perpetuity.

The various states of the Union and, quite recently, the various states of the Commonwealth, accepted similar consolidations in spite of a similar dread on the part of the newer regions of the industries of the older. The truth is that the human animal appears to be so constituted that the intervention of 'the salt estranging sea' acts on his imagination in such a manner as to create an almost invincible separatist sentiment. It appears to be a far more effective separator than original differences of race, language, or faith. Rome pushed on its gradual expansion by land, and found in the end its most vigorous enemies, as in the case of the Arverni, converted into its most ardent patriots. Corinth despatched a group of its own citizens to occupy a neighbouring island, and found them in a few years converted into the most virulent of its enemies. The ties between the mother city and its colonies in and about the Ægean were always of the slenderest character. With regard to our own oldest colonies, it is probable that the most judicious Government conceivable would not much longer have retained their allegiance. Montcalm, as we know, found them already, in his day, prepared to throw off the English yoke as soon as the English arms should have relieved them from the dread of French conquest. No doubt the wiser policy of the last hundred years has made the colonial sentiment of the present into a very different thing from the colonial sentiment of the eighteenth century. Many years, perhaps many centuries, however, will have to

pass, if we may judge by present appearances, before either Canada or Australia will come so far to regard Great Britain as one with itself as to welcome the unrestricted competition of English goods with its local manufactures. Unification in that sense may probably be dismissed as far outside the range of practical politics. All things considered, we shall probably do wisely to be content with measures calculated to maintain and, where possible, to improve the excellent relations at present existing, between Great Britain and her daughter nations, rather than to pursue the shadow of close commercial consolidation.

CHAPTER XXV

INTERNATIONAL COMPARISONS

THE Tariff Reform controversy, if it has not led to legislative results, has, at any rate, given a new impulse to economic thought. It has made us all busy with comparisons between our social conditions and those of our neighbours, comparisons that may bring with them in the end even more enlightenment on other questions than on the fiscal one. We may glance briefly at some of the most interesting features of these comparisons.

Our Commercial Position.—As to ourselves, the future historian, when he addresses himself to the task of describing the commercial conditions of Britain at the beginning of the twentieth century, will be able to say that at this period half the shipping on the ocean carried her flag, that in the cotton industry she owned and worked nearly half the spindles in the world, that her exports were close upon £10 per head of population as compared with figures ranging between £6 and £4 for Germany, France, and the United States. He would find again that in forty years the income of the income-tax-paying classes had much more than doubled, that wages in many cases had doubled also, and in all had largely increased, while the necessaries of life and the comforts and luxuries of the poor had almost, without exception, been very greatly cheapened. As regards corporate wealth and striking power, he would remark that the England of the early twentieth century aimed steadily, and with a fair degree of success, at keeping on the seas a fleet that should be a match for the fleets of any two of her rivals, an amazing feat surely when it is recognised that she was confronted with competitors as

civilised as herself, and whose populations vastly outnumbered hers.

After having made such observations as these the historian would, no doubt, expect to find the treatment of the subject in the contemporary Press impressed with a sentiment of self-congratulation, and would probably be more than surprised to discover that just the opposite of this was the case, that, on the contrary, many of the most important newspapers appeared to be possessed by the idea that British commerce was in the midst of a period of universal decadence, and that nothing could save it from complete destruction but a thoroughgoing change in the fiscal system.

Turning to another aspect of the matter, his surprise would probably also be considerable to find that the Englishman of to-day, while constantly increasing his wealth, and consequently his liability to be mulcted in huge war-indemnities, declined, for reasons not easy of explanation, but connected, apparently, more or less closely, with the nature of the religious teaching prevalent in the country, to follow the example of the rest of Europe in training the manhood of the nation to the use of arms.

Comparison with the United States.—As to the comparison of conditions in Great Britain with those ruling in the United States, it is obviously one very difficult to apply in such a manner as to draw any valid conclusions from it. No one really doubts that in such countries as America, and as most of our self-governing colonies, wages would be much higher under any fiscal system than they could be expected to be anywhere in Europe. The explanation of this fact generally given and accepted is that these countries are ' new ' countries, and no doubt it is one that roughly corresponds to the truth. It seems worth while, however, to inquire why it is that the fact of a country being ' new ' is so generally accompanied by the fact of its possessing a high rate of wages and interest. The assertion certainly cannot be made that the coincidence is universal, or that the newer a country is the higher are the wages likely to

be. There are people still living, both in New Zealand and in parts of Australia, who can look back to a period when wages stood at about half their present figures, and the recent development of the cotton industry in the southern States of America has revealed to the world the existence of very cheap labour there.[1] Nor can the fact be accounted for simply by telling us of the bounty of nature and the facility with which land can be obtained. There are islands in the Pacific where all that is wanted for bodily necessities can be had for nothing, but where, at the same time, the wages that it would be possible for any one to earn would be as close as possible to zero. It seems to be the case thus that in order to bring about the prosperity generally associated with 'newness' the coincidence of more than one condition is requisite. In Australia, after Macarthur introduced the merino sheep, there was, it is said, a period during which every £1000 that a man put into the pastoral industry was likely, with ordinary luck, to bring him in £1000 a year. In such circumstances, or anything approaching them, we may be sure that the pastoralist would not worry much either about the rate of interest that he had to pay for his money, or the wages that were demanded for the labour that he had to employ, but would take all that he could get of either on anything like reasonable terms. Wages would no doubt long ago have risen to their present figure in Australia, though never an ounce of gold had been found either at Bendigo or at Ballarat.

When I first went to New Zealand in 1867, a condition of affairs more or less parallel to the above was the prevailing one. Land that, owing to its character and to the mildness of the winters, was intrinsically more valuable for grazing than any English land, could be obtained either from the State or the natives at rents that would have formed but a fraction of the Home rent. Sheep were worth about £1 a head, and, with land in abundance, they could be doubled, or nearly doubled, in number every year. Wool

[1] Piece-work is, or was recently, taken at rates that were about one quarter of the Lancashire rate.

stood at prices much better than the excellent prices that rule at the present moment.[1] In these circumstances it is not surprising that the runholders contentedly, and with quite satisfactory results to themselves paid, year after year, ten and even twelve per cent. for the money that they used ; and that the labourer immigrant, on landing, found that he could command at least double the wages that he could have obtained at Home—as indeed he still can, after all the changes that have taken place. Retail prices responded, of course, in a marked manner to the high range of profits and wages, rather, however, as regarded specialities than as regarded the regular expenses of housekeeping. Each glass of beer or whisky cost 6d., yet the enterprising squatter, when he visited the hotel in the nearest township, and desired to entertain his friends, and to advertise his prosperity, would call for ' a bucket of rum and pannikins.' That practice, however, it must be said, belongs to an earlier day than that which fell within my experience. Coppers, in Napier, the port of Hawkes Bay, in 1867, were unknown. A pencil, or the like, that you could get at home for a penny, would cost you sixpence. Sixpence, indeed, was practically the lowest coin in use. A good many of the phenomena thus, it appears, that ordinarily accompany the opening of a successful goldfield, and which the quantitative economists associate exclusively with discoveries of gold, had, in that purely pastoral centre, come into existence. If money was plentiful there, that was solely because the sale of the staple produce at good prices at home had brought it to New Zealand in considerable abundance.

Two leading conditions, it will thus be seen in such a case, co-operate to bring about the prosperity of the ' new ' country ; first, cheap land ; and, second, access to the markets of the old world. Take away the latter, and rough abundance indeed might rule, but no one would make his fortune, nor would the wages of labour conspicuously rise. We may generalise the statement, and say that what is necessary is the cheapness of one of the factors of the pro-

[1] December 1911.

duction of some staple product—the factor in this case being the land, the product wool—together with the maintenance or approximate maintenance of the price of this product.

Keeping this principle in mind, we may look at some other aspects of the comparison between British and American economic conditions. In the case of such industries as wheat and wool production, we have seen that it is plain enough how the rate of wages in the new country comes to be higher than that ruling in the old. There are other industries, however, in regard to which a more complex explanation is needed to make the phenomenon comprehensible. How is it, we may ask, that the rate of wages paid in the boot-making trade in America is about double the English rate, while, at the same time, the American boot manufacturers can compete with us with considerable success even in our own markets? Cheap land is not the explanation here, as the land on which boot factories are erected is not cheap. The Tariff Reformer, of course, has his answer ready. The fact, he contends, is due to Protection. But, the reply has been many times given and never answered, if it is Protection that has raised American wages in manufacturing industries to a figure far above the English rate, how is it that, in protected France and Germany, such wages still lag far behind it? Clearly we must look elsewhere for the explanation of the facts. It may, of course, be argued that the high rate of wages in America, in agriculture, due to causes that are readily enough comprehensible, maintains the general rate of wages in the country, inasmuch as men will not take low wages in one industry while they can get high wages in another. That is both true and important, but it still leaves unexplained the fact that the American manufacturer can afford to pay those high wages while he is yet able to sell his product in neutral markets at lower prices than the similar products of countries where much lower wage rates prevail; and to do this not only now and then, when accumulated stock has to be got rid of, but regularly and steadily year after year. There seems to be no explanation of this fact possible, apart from

the admission that, from some cause or other, in many departments of production at any rate, American industry is vastly more efficient than ours. Where, again, however, have we to look for the source of this superior efficiency ? It is not apparently to be found in the innate qualities of the operatives. No workman is more efficient, by the general testimony of the American manufacturers themselves, than the English workman when he emigrates to America. The superiority, it seems, can lie nowhere else but in the organisation of industry. We are familiar with the fact that the American manufacturer as a rule, though not always, much more readily scraps his old plant in order to replace it with new, than does the Englishman similarly situated. We have to ask again, however, how does this fact take its origin ? Are there circumstances discoverable that assist in any way to explain it ?

The explanation is perhaps, to some extent, to be found in the fact that the Americans are in advance of us in the scale of their industries, that those great Trusts, in short, that are so unpopular with large sections of their own population are, in no small degree, the cause of the immense industrial efficiency of the nation. Mr. Carnegie, in his evidence before the American Tariff Commission, expressed the opinion that steel could now be produced much more cheaply in America than anywhere else in the world, and attributed this to the fact that the various processes necessary in order to convert the ore into pig iron, and again to convert the pig iron into steel, were carried on in America continuously under one roof, the metal never being allowed to cool from first to last. The necessity for great accumulations of capital in order to make cheap production possible is, no doubt, specially conspicuous in the iron industry, but tells in innumerable other industries as well.

Trade Unionist Policy.—This fact again, beyond question, is due in some measure to the circumstance that the great establishments are in a far better position for resisting the interference of the trade unions with the manage-

ment of their business than are the smaller ones. As to the claim so frequently put forward on behalf of the trade unions that they have been the agency that has raised the general rate of wages in this country in the past, it is interesting to note what is the opinion on that point of the one man of genius in England who professes the Socialist faith, Mr. G. B. Shaw. In speaking of the decade 1850-60, he remarks, 'Wages went up; and the unions like the fly on the wheel, thought that they had raised them.'[1] The views on this point that have been set forth by the able Glasgow economist, the late Mr. T. S. Cree, are well worthy of attention. While willing to concede to the utmost the excellent intentions of the promoters of the Trade Union movement, he is of opinion that the whole conception at the root of collective bargaining is fundamentally unsound. In the commodity markets, under modern conditions, the producers of wheat, or cotton, or wool, put their produce on the market, and let it go always for what it will fetch. Experience teaches them that they will thus come out better in the long-run than by holding it over for long periods in the hope of better prices.

The same principle, in his opinion, applies to labour. In the occupations, such as domestic service, in which, from the nature of things, no Trade Union can exist, wages appear to have enjoyed a fuller share of the general rise that has been in progress in recent years than in any others. Mr. Webb, indeed, by a line of reasoning which it is not easy to follow, maintains that domestic service is not a case in point.[2] The truth is, that it is so completely a case in point that the argument from it to other occupations is an *a fortiori* one. The mistress who desires to add one more to her already ample staff of servants, is evidently in the strongest possible position to refuse any demand for wages which she does not choose, of her own free will, to comply with. The sacrifice involved in doing without the services offered is so small as to be, to all intents, non-existent. If, for all that, wages among the servants of the rich are always

[1] *Fabian Essays*, p. 185. [2] *Industrial Democracy*, ii. 6.

on the rise, as indeed they are, the conclusion to which the fact points is that it is to invincible natural forces rather than to labour organisation that we have to look for the explanation of the rise in wages generally. Of course no one doubts that if you take the case of any particular trade, the union, it will be found, can, for a time at any rate, raise the rate of wages in it by limiting the number of those that are allowed to enter it ; but, as regards the country generally, the particular gain is here balanced, and probably far more than balanced, by the general loss.

Mr. Webb quotes instances in which, as he remarks, the policy of the unions has conduced to the increased efficiency of industry, and thus in the end raised wages, and it is significant that his argument here assumes the validity of the principle that the raising of profits will raise wages in the end. The masters, he contends, have been frequently forced by the onerous conditions imposed by the unions into the adoption of labour-saving appliances, to which they would not otherwise have resorted. This, no doubt, may happen in some cases, but the line of reasoning is surely a surprising one. Any advantage that industry may gain, in such circumstances, is gained not in accordance with the desires and intentions of the unions, but in spite of their hostility. It is due to developments that they did not anticipate, and which, if they had anticipated them, would have caused them to alter their policy. It reminds one of the argument that because the world could not have been redeemed without the intervention of Judas and Pilate, the reverential gratitude of humanity is due to these personages. The unions, no doubt, in such cases might say with Mephistopheles, 'We are the influence that always wills the evil and always brings about the good.' The worst of such a line of reasoning is that you cannot make any practical use of it. We may agree with any one who asserts that Napoleon, by overthrowing the German armies, and occupying Berlin and Vienna, caused the new birth of German patriotism, and contributed in no small degree to the creation of the mighty empire of the Hohenzollerns. We cannot, however, seriously desire, for such a reason,

that our armies should be defeated, and that London should be occupied, though the result might be that the English nature would be renovated, and that Britain in the end would be made as vigorous and as virile as she was in the days of Elizabeth. Nor, similarly, with regard to the trade unions, can we reasonably wish to see their policy pushed on more vigorously than hitherto, on its present lines, in order that the manufacturers should be driven into adopting yet more and more effective labour-saving appliances, in order to defeat it.

Comparison with Germany.—So much, then, as to the comparison of our industrial conditions with those ruling in America. As regards Germany, a line of thought that is in some respects different, suggests itself. When we compare the present condition of the labouring classes in England with that of the same classes in Germany, two facts emerge distinctly enough from the maze of contradictory figures and varying general testimony; first, that the Englishman gets very much better pay for shorter hours of work than the German; secondly, that the German is, on the whole, both better clad and better nourished, and that the slum and the tramp, so much in evidence with us, are both in Germany practically unknown.

In attempting to diagnose the causes of relative national health and soundness, we have to look at the life of nations as a whole, and certainly we must not omit to take into consideration the attitude of the people towards all that is embraced under the conception of religion. In describing social conditions in Central Italy during the last years of Pius IX., a recent writer says: 'The Papal Government must be pronounced a failure even by favourable critics. . . . Yet the system itself was not bad in its intention, but good. It assumed the rule of Christ as a first and pervading principle of government; and the rule of Christ's Vicar was an attempt to carry out in practice the spirit and precepts of the Gospel. Hence the profuse and reckless charity, with the consequent pauperisation, beggary and idleness. . . . As a consequence Rome, like all holy cities, was incredibly

filthy.'[1] There seems, indeed, to be some danger to the social health of a nation in the too great absorption of influential classes in the other-worldly aspects of religion, and the comparative neglect of those which bear on the love of one's country and loyalty to one's sovereign. The old religion of Judea, as well, of course, as the religions of Greece and Rome, were closely identified with such love and loyalty. 'Whatever can be said of Christianity,' says Mr. Swinburne, in one of his recently published letters, 'it cannot be said that it is a patriotic religion.' But the Germans are assuredly as profoundly Christian as we are, and the type of Christianity that prevails among them is certainly a type with which no fault can be found on the score of deficiency in the patriotic sentiment.

Germany, we are often told, has forsaken the tradition of the early nineteenth century. She is so absorbed in the race for wealth that reflection on the outlook of humanity, and on the universe present and to come, has ceased altogether to be a matter of concern to her. No race or people, however, thus suddenly changes the most fundamental features of its character. The reflection, the idealism, is there undoubtedly still, and has perhaps penetrated more deeply than ever into the fibre of the nation. Among its results is the fact that the eschatological conceptions which made their way into the Hebrew religion in the second and third centuries before Christ no longer fill her horizon as they still do our own. These are, however, as we know, the conceptions that, in the Roman Empire, at the crisis of her fate, drove the best elements in the population, the men who, in other circumstances, would have most unhesitatingly sacrificed themselves for their country, into the cloister and to the desert; and, in the opinion not only of Gibbon, but unless my memory fails me, of so judicious a Christian historian as Dr. Hodgkin, made the barbarian conquest inevitable. What has taken their place in Germany, in the minds of all those who are most vividly impressed with the shortness of life and the futility of mere selfish worldly success, is nothing else but the passionate desire for the

[1] *Spectator*, 15th January 1910.

prosperity and the greatness of the Fatherland. The patriotic sentiment has, in all ages, been the most effective antiseptic of society, and it is, perhaps, in no small degree to its dominance there, and its atrophy here, that is due the fact that the comparison in respect of social conditions results so unmistakably in favour of Germany. If Franke and the Pietists had succeeded in obtaining the same hold on the German mind in the eighteenth century that the revived Puritanism obtained over the English mind during the same period, one cannot help wondering whether Germany would now have been an armed nation with practically every unit in her male population ready at a moment's notice to face death in defence of her hearths and homes, and again, whether her social conditions would be so different from our own as confessedly they are.

Turning to the special question of unemployment, it is probably the case that indiscriminate almsgiving, and the temper akin to it that is frequently manifested in the management of our Poor Law Institutions, are the main causes of the bad showing that we make as compared with some other countries as regards the ranks of casual labour. When we read of occurrences like the Poplar scandals, we may be ready perhaps to jump to the conclusion that things in this respect are steadily going from bad to worse. On a historical retrospect, however, this is at once seen to be very far from the truth. The present attitude indeed of educated modern sentiment towards almsgiving is really a new thing in the world. We hear much of the mischievous results that were associated with the cry of *panem et circenses* in Rome. It would probably be found that the emperors who, to our thinking, were the worst culprits in that matter were not actuated solely by the selfish aim of bribing the populace but, in part, by misplaced sentiment. When Aurelian quadrupled the doles of the soldiers and burnt the obligations of the State debtors, he may have looked on the proceeding as good business. There is little doubt, at the same time, that, in contemplating his own action, he himself felt a thrill of self-approval, and agreed probably with his whole heart, with every word that the

State panegyrist had to say on the subject. At the Christian era, and all through the Middle Ages, almsgiving, as we know, was looked upon as the most sacred of all duties. If it was only indiscriminate enough and lavish enough, its reward was elevation to the ranks of the sainthood. As regards the present, it is perhaps hardly going too far to affirm that the day is in sight when it will be absolutely prohibited in every civilised state. The change of view on the part of modern nations upon this and other closely kindred questions, is perhaps the greatest achievement of economic science, and economic science is here, at any rate, synonymous with enlightened common-sense.

Wages Higher in England, but Employment Less.—So much then as regards unemployment as affecting the lowest class of labour. It will be rejoined, however, that it is not only as regards such labour that the comparison with Germany results unfavourably for us, but also as affecting the members of trade unions. Granted that lower wages, but more regular employment rule in Germany, higher wages but less regular employment in England, the question, of course, at once arises, are not these two facts two aspects of the same phenomenon, are not both to be explained indeed by the greater power of the trade unions in England. Under the rule of those bodies, the most highly skilled labour probably fares better with us, the less skilled better with them. That is certainly the conclusion that would present itself as obvious to the mind of any investigator who was led to view the facts for the first time.

Occasionally an incident crops up which brings into a strong light the incompatibility between a rate of wages maintained above the economic level and the existence of such facilities for employment in a country as we should desire to see. It may be in the remembrance of some of my readers that, a year or two ago, when unemployment was at its worst, one of our newspapers took the step of sending a reporter to accompany an unemployed fitter, who was in search of a job. There was no doubt as to the

man's *bona fides*. He was at it from morning till night, making his applications for work at the offices of the various establishments, but without any success. It transpired, however, that he could have got a job over and over again at 28s. per week. He was not permitted, however, by his trade union to accept one at anything under 30s. If he did so, he forfeited all the benefits due to his past payments. This appears to be the rock on which the unemployment insurance project can hardly fail to make shipwreck. It is impossible to believe that State-aided out-of-work benefit can ever be granted to men who are offered very excellent wages, yet such as do not satisfy the demands of the unions. At the same time, of course, all organised labour would be up in arms against any proposal which might make the minimum wage prescribed by a trade union subject to review by the Courts. To enact such a proposal, indeed, would be equivalent to the suppression of the unions.

Conclusion

The Labour Question.—Our essay at international comparisons has led us into speculations and reflections mainly connected with the labour problem. We may fittingly conclude the chapter and the book with a few further observations specially directed to that subject.

To those who viewed from a detached standpoint the course of events in connection with Lord Furness's offer to the shipwrights of Hartlepool of a share in the profits of Furness, Withy and Co., it must have come as an immense surprise to find that, after the men had accepted the arrangement, and had seen it carried out for a year with results completely satisfactory to themselves, they, in the end, nevertheless, decided to withdraw from it. They did so, no doubt, as the result of pressure brought to bear on them from outside. That such pressure, however, should have been brought to bear, and that they should have yielded to it are facts that afford convincing testimony to the strength of the feeling among the trades unionists in the country generally as to the desirability, and even the

necessity, of keeping the forces of labour continually arrayed in a hostile camp over against the forces of capital.

The sentiment is based on the Marxian doctrine that capital is continually engaged in appropriating wealth that of right belongs to labour, and that it should consequently be the constant end and aim of the organisation of labour to recover from it some of this misappropriated wealth.

Those who pin their faith, however, to the hostile camp theory and the necessity of making it perpetual, should at any rate reflect that, for relations of mutual antagonism, the relations between labour and capital have some strange peculiarities. In any other conceivable case of hostility one enemy stands always to gain by the diminution of the numbers and resources of the other. But in the case of labour and capital this situation is reversed. Labour stands to gain, not by the diminution but by the increase of capital and of capitalists in the country. Even the moderately intelligent labourer in practical matters dreads nothing so much as the closing of works and the migration of capitalists to other countries, or to other parts of the same country.

All this points to the conclusion that the really dominant fact of the situation is not the hostility between labour and capital, but the solidarity of their interests. It coincides, too, with the view already expressed more than once, to the effect that there is only one way of increasing the wages of labour in any nation on a considerable scale, and that is, by first increasing the profits of capital.

It is interesting to observe over how wide a field this latter and sounder view already makes its influence felt. It is often said of the Tariff Reform movement that Protection is but a phase of Socialism ; and no doubt the two have this much in common, that they both repose immense faith in State intervention. There is, however, this great difference between their respective standpoints. The Socialist has but one conception in regard to wages, and that is the conception that their augmentation is only possible

at the expense of profits. The Protectionist, on the contrary, frankly takes it for granted that the only method worth considering for raising wages is, in the first instance, to raise profits.

Much the same may be said of the Free Trader, from his own point of view. The vote recorded by Lancashire in favour of Free Trade bore eloquent testimony to the faith of the operatives in the solidarity of their interests with those of their employers. The maintenance of Free Trade, they felt, was an essential condition of the continued prosperity of the cotton manufacture in their county, and with the prosperity of the manufacturer it stood to reason, in their view, that the prosperity of themselves, the operatives, must stand or fall.

When a true conception and a false one are thus together in the field, we may take it as fairly certain that, in the end, the true one will come out the winner. It may take years, decades, even centuries for it to establish beyond question its right to dominance, but it will not fail to do it in the long-run. Monetary history, we have seen, is full of fallacies, once dominant now discarded. If one had lived in the days of Philip the Fair, he might well have been excused if he had doubted whether the right of the sovereign to debase and diminish the money would ever have been surrendered. In the days of Colbert even, one might still have been uncertain on that point ; yet now the money is debased nowhere in the world, unless indeed it be in China. Parallel follies, too, such as over issues of paper money are, we know, daily growing rarer. What has happened in the case of monetary fallacies may yet happen in that of those less specialised ones, the prevalence of which now troubles the non-socialistic economist. It is, at any rate, conceivable that our descendants of two or three centuries hence may hear a great deal less than we do about restrictions of the output, about the redistribution of wealth, or about the State ownership of the means of production.

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